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THE

SCIENCE OF FINANCE

"Upon a perfect knowledge and right appreciation of details, the settlement of Great Questions mainly depends."

—*Disraeli.*

"What I want is, Facts."

—*Boz.*

THE NATIONAL BANK OF SCOTLAND EDINBURGH

THE

SCIENCE OF FINANCE

A PRACTICAL TREATISE

BY

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"When I recollect that the great majority of the population of the United Kingdom rise every day dependent for their subsistence—their daily subsistence—on their daily labour; when I recollect the delicate marvel of our Credit—more wonderful, in my opinion, than our accumulated Capital; when I know that not a sun rises upon a British Minister that does not bring him care, and often inexpressible anxiety, . . . a collapse of credit, a declining trade, a decaying revenue, . . . I declare I often wonder where is the strength of thought and the fund of feeling that are adequate to cope with such colossal circumstances."

—THE CHANCELLOR OF THE EXCHEQUER AT EDINBURGH, Oct. 1867.

PREFACE

THIS book completes the exposition of the subject which I began in my work on the "Economy of Capital." The importance of the subject can hardly be overrated. A good Financial system is the chief adjuvant of Industry—of the growth of wealth and of social wellbeing. It furnishes "the sinews of war," which give power to a State when compelled to combat with its neighbours; it at the same time promotes peace and contentment at home,—strengthening alike the political and the social fabric of a community, by furnishing ample work for all classes, and especially for the millions who rise every morning dependent on the coming day's labour for their daily food. It will tend to diminish the poor-rates, as well as thin the ranks of the costly criminal class. Crime and disloyalty are in great part the offspring of suffering and of want.

The first chapter of the work gives as it were a bird's-eye view of the marvellous Credit-system established in our country,—which, through the medium of Banking and other financial processes, not only economises the reserve-wealth of the community, by gathering it into reservoirs, but vastly increases its effective power as a means of production. I next consider the other starting-point of my subject,—namely, the Trade which is the giant offspring of this marvellous Credit-system. One chapter is devoted to the Balance of Trade,—showing how this balance is constituted, and in what manner it is liquidated: a matter of much interest of itself, and still more so owing to the incorrect ideas prevalent on the subject.

In the second section of the work, "Capital" is treated of in its various forms and conditions, —as Fixed, Floating, and Loanable. In the interspersed chapters on the "Economy of Force," the "Potency of Capital," and the "Negotiability of Value," are unveiled the *principles* which underlie the Credit-system, and which serve to multiply capital by increasing its effective power.

From Loanable Capital we proceed naturally to the Rate of Interest—which is one of the cardinal and most important practical points in Fin-

ancial Science. And here we come face to face with a great evil to which this country is subjected—namely, violent fluctuations in the Rate of Discount, *i. e.*, the charge for money on loan. As the rate of discount is necessarily affected by Banking and Commercial embarrassments, we next consider such cases, and inquire in what way and to what extent a banking or commercial crisis, or both together, legitimately affect the rate of discount.

From this we proceed to pass in review the Monetary System of this country,—showing its varying conditions from its first establishment at the close of the seventeenth century down to the present time. The working of the existing system, as regulated by the Bank Acts of 1844-5, is fully described, alike in ordinary times and in periods of exceptional difficulty. A chapter is devoted to the monetary crisis which accompanied the great Panic of 1866.

After a review of the Banking and Monetary systems established in foreign countries, we proceed to consider by what means our own monetary system can be brought into harmony with the spirit of the age and the wants of the community. This subject is fully discussed in Chapters XVIII. to XXII. And we close this section of

the work by proposing an International Monetary System, as an important means of benefiting the trade and improving the material interests of all countries.

The next section of the work relates to the effects of Government Taxation, and of a National Debt; and as regards our own country, the question is discussed how far it is expedient to pay off any portion of our Debt, and in what form such extinction of the debt can best be accomplished.

Railway Finance is an affair of such magnitude, and at the present moment a matter of so great interest, that two chapters are devoted to its elucidation,—containing an exposition alike of the faults of the past, of the present defects, and of the various remedies which are urgently needed.

Municipal Finance — the methods by which towns and cities can employ their financial resources in a manner beneficial to their own communities—is next considered. It is a development on a large scale of the system of Co-operative Societies. We then come to the great question of Land-Credit—to the means by which our Credit-system, so marvellously developed as regards commercial securities, may be extended in an approximately equal degree to that most

stable and important form of national property, the Land and Agriculture.

In conclusion, passing from pure Finance partially into Politics, we consider the duties which the State, as the representative of the Nation, owes to the poor,—the means by which it may aid the lower classes in raising themselves in the social scale, and still more, in obtaining employment for their labour, which is their only capital. In this chapter, also, we suggest various methods by which the resources of the country may be more fully developed, either by private enterprise, or with the help of the State, by turning to account some sources of national wealth which are at present neglected and unproductive.

Such is the scheme of the present work,—a work embodying the fruits, and in which are condensed the labours, of many years of careful study and investigation. My best hope is, and my amplest compensation will be, that its usefulness to the community may in some degree correspond with the amount of earnest and long-continued labour bestowed upon it.

December 30, 1867.

ERRATUM.

On p. 36, delete the footnote "† See *infra*, Chap. V."

CONTENTS

CHAPTER I.

PAGE

OUR INVISIBLE CAPITAL, ... 1

METHODS OF STORING RESERVE-WEALTH, . . . 7

ORIGIN OF MONEY, ... 10

ORIGIN OF BANKING, ... 12

ORIGIN OF PAPER-MONEY, ... 14

ECONOMY OF BANKING, ... 22

ECONOMY OF BANK-NOTES, ... 23

THE CHEQUE-SYSTEM, ... 25

THE CLEARING-HOUSE, ... 26

ECONOMY OF THESE PROCESSES IN THE STORING OF RESERVE-WEALTH, ... 28

BILLS, ... 30

HOME BILLS, ... 31

FOREIGN BILLS, ... 32

SMALL PART WHICH COIN AND NOTES PLAY IN OUR FINANCIAL SYSTEM, ... 34

CHAPTER II.

ABSORPTION OF SPECIE, ... 39

IN INTERNATIONAL TRADE, ... 41

IN THE HOME CIRCULATION, ... 42

BY THE BANKS, ... 43

CHAPTER III.

INTERNATIONAL TRADE, ... 46
FOREIGN TRADE OF FRANCE AND ENGLAND, . . . 48
COMPARATIVE STATEMENT, ... 49
TRANSIT-TRADE OF THOSE COUNTRIES, ... 51
BALANCE OF THEIR EXPORTS AND IMPORTS, . . . 53
FOOD-TRADE OF FRANCE, ... 54
FOOD-IMPORTS OF ENGLAND, ... 55
TRADE-BALANCES OF FRANCE AND ENGLAND COMPARED WITH THEIR IMPORTS AND EXPORTS OF SPECIE, . 57

CHAPTER IV.

THE BALANCE OF TRADE, ... 59
EXCESS OF OUR IMPORTS OVER EXPORTS, . . . 60
A GREAT PART OF THIS EXCESS IS MERELY APPARENT, . 61
TRUE STATEMENT OF OUR TRADE-BALANCE, . . . 63
THE FINANCIAL BALANCE, ... 64
BALANCE OF IMPORTS AND EXPORTS OF SPECIE, . . 66
CONCLUSION: CONJECTURAL ESTIMATE, ... 68

CHAPTER V.

WHAT IS CAPITAL? 70
NO CLEAR DEFINITION OF THE TERM YET GIVEN, . . *ib.*
AS USED BY JAMES WILSON, ... 73
BY MILL, ... *ib.*
BY M'LEOD, ... 75
IS MONEY CAPITAL? 76
MONEY IN BANK, ... *ib.*
MONEY IN CIRCULATION, ... 77
ARE BANK-NOTES AND BILLS CAPITAL? 79
SUMMARY OF OPINIONS, ... 81
OUR DEFINITION OF CAPITAL, ... 83
DIFFERENCE BETWEEN NATIONAL AND INDIVIDUAL CAPITAL, 84

OUR PRIMARY DEFINITION, ... 86
SECONDARY DEFINITION, ... *ib.*
SAME AMOUNT OF CAPITAL MAY HAVE WIDELY DIFFERENT PRODUCTIVE POWER, ... 88

CHAPTER VI.

THE ECONOMY OF FORCE, ... 90
AN INDISPENSABLE REQUISITE OF CIVILISATION, . . *ib.*
ITS INTRINSIC VALUE REMAINING THE SAME, A THING MAY BE MADE TO POSSESS AN INCREASED POWER OF PRODUCTION, ... 92
EXAMPLES OF THIS, ... 93

CHAPTER VII.

THE POTENCY OF CAPITAL, ... 98
PARALLEL BETWEEN ROADS AND MONEY, . . . *ib.*
ECONOMY OF PRODUCTION EFFECTED BY ROADS, . . 99
DO. DO. DO. BY MONEY, . . 101
THE PRINCIPLES OF MONEY AND BANKING, . . . 103
CAPITAL MOST POTENT WHEN IN FEW HANDS, . . 106
THE DIFFUSION OF CAPITAL SOCIALLY ADVANTAGEOUS, . 107
BANKS TAKE THE PLACE OF LARGE CAPITALISTS, . . 109

CHAPTER VIII.

NEGOTIABILITY OF VALUE, ... 111
DIFFERENCE IN THE NEGOTIABILITY OF THE VARIOUS KINDS OF PROPERTY, ... *ib.*
NEGOTIABILITY ADDS TO INTRINSIC VALUE, . . . 112
HOW IS NEGOTIABILITY IMPARTED? 113
COMMERCIAL CURRENCY, ... 114
BANKING CURRENCY, ... 119
FINANCIAL CURRENCY, ... 124
EFFECTS OF THIS SYSTEM, ... 128

CHAPTER IX.

FIXED AND FLOATING CAPITAL, ... 129
NECESSITY FOR A CLEAR TERMINOLOGY, ... *ib.*
FLOATING CAPITAL, ... 132
EXAMPLES, ... 133
FIXED CAPITAL, ... 134
EXAMPLES, ... 135
EFFECTS OF A "FIXING" OF CAPITAL, ... 136
EXAMPLES, ... 138
CONCLUDING REMARKS, ... 141

CHAPTER X.

LOANABLE CAPITAL, ... 145
WHAT IS LOANABLE CAPITAL? 146
THE POWER OF BANKS TO MAKE LOANS, ... *ib.*
WANT OF LOANABLE CAPITAL MAY BE DUE TO THE PUBLIC, 147
OR IT MAY EXIST ON THE PART OF THE BANKS, . . *ib.*
EXAMPLES, ... 148

CHAPTER XI.

BANKING EMBARRASSMENTS, ... 150
A RUN ON THE BANKS FOR SPECIE,—DEPOSITS, . . 151
SMALL PART WHICH A CASHING OF NOTES PLAYS IN SUCH RUNS, ... *ib.*
EXTERNAL DRAINS OF SPECIE, ... 154
CHARACTER OF THOSE DRAINS, ... 155
THEIR NATURAL LIMIT, ... 156
DO NOT PRODUCE A CASHING OF NOTES, ... 158
CAUSE OF EXTERNAL DRAINS, ... 159
NOT USUALLY A SIGN OF NATIONAL INDEBTEDNESS, . 160
HOW THE SPECIE IS WITHDRAWN, ... 162
EFFECT OF EXTERNAL DRAINS ON THE BANKS, . . 163

DEFENSIVE MEASURES OF THE BANKS, ... 164
THE OLD SYSTEM, ... 165
THE PRESENT SYSTEM, ... 166
INEFFICIENCY OF THE PRESENT SYSTEM, . . . 167
THE PROPER COURSE, ... 168
INTERNAL DRAINS—FOR NOTES OR COIN, . . . 170
HOW THEY TAKE PLACE, ... 171
A COMMERCIAL CRISIS, ... 173
A BANKING CRISIS, ... 176
REMEDIES FOR INTERNAL DRAINS, ... 177
SYSTEM OF BANKING CO-OPERATION, ... 179

CHAPTER XII.

THE RATE OF INTEREST, ... 182
HOW A SCARCITY OF MONEY AFFECTS RATE OF INTEREST, 186
EFFECTS OF A HIGH AND LOW RATE OF INTEREST, . 189
THE BANK-RATE, ... 191
HOW IT IS AFFECTED, ... 192
EXAMPLES, ... 193
THERE OUGHT TO BE NO MONOPOLY OF BANKING-CURRENCY, 199
AND NO NEEDLESS RESTRICTIONS ON ITS ISSUE, . . 200
AN ILLUSTRATION, ... 201

CHAPTER XIII.

OUR MONETARY SYSTEM, ... 203
PRACTICAL WORKING OF THE BANK ACTS, . . . 204
THEIR PERMANENT EFFECTS, ... 206
GREAT TEMPORARY DIFFICULTIES WHICH THEY OCCASION, 209
THE TIDES IN THE CURRENCY, ... 211
THE ANNUAL MONETARY CLIMACTERIC, ... 213
SEMI-CRISES OF OCTOBER 1864 AND 1865, . . . 214
THEIR EFFECTS ON THE BANK, ... 215
NO FOREIGN DRAIN OF GOLD, ... 217
EXCESSIVE ELEVATIONS OF THE BANK-RATE, . . 218

CHAPTER XIV.

THE PANIC OF 1866, ... 222
PRELIMINARY DISQUIET, ... 223
FALL OF THE JOINT-STOCK DISCOUNT COMPANY, . . 224
ORGANISED "BEARING" OPERATIONS, ... 225
PARALLEL IN THE UNITED STATES IN 1857, . . . 227
RECKLESS "FINANCIERING" OPERATIONS, . . . 228
FALL OF OVEREND, GURNEY, & CO., ... 231
PANIC IN THE CITY, ... 233
INADEQUATE SUPPLY OF CURRENCY, ... 234
POSITION OF THE LONDON BANKS, ... 235
SUSPENSION OF THE BANK ACT, ... 237
BANK REFUSES TO ENLARGE ITS NOTE-ISSUES, . . 238
CONTINUANCE OF THE PANIC, ... *ib.*
FALL OF OTHER BANKS AND COMPANIES, . . . 239
MAGNITUDE OF THE DISASTER, ... 240
THE BANK HAD THE FIELD TO ITSELF, ... 241
IMMENSE INCREASE OF ITS PROFITS, ... *ib.*
ITS CONDUCT GREATLY HEIGHTENED THE DISASTER, . 242
BAD FORM IN WHICH THE ACT IS SUSPENDED, . . 244
AN UNJUST FAVOUR TO BANK OF ENGLAND, . . . 245
NO FOREIGN DRAIN OF GOLD, ... 248
BLUNDERS OF THE GOVERNMENT, ... 249
ABSURD CONDITIONS ON WHICH IT SUSPENDS THE ACT, . 250
NO WANT OF GOLD IN THE BANK, ... 252
DAMAGE TO OUR NATIONAL CREDIT, ... 253
REFLECTIONS ON THE CRISIS, ... 254

CHAPTER XV.

IMPOLICY OF THE BANK ACTS, ... 255
THE BANK DIRECTORS AND THE ACT, ... 256
PROFITABLENESS OF THIS COURSE TO THE BANK, . . 257
SYSTEM CONTEMPLATED BY SIR R. PEEL, ... 258
OPPOSITE PRACTICE OF THE DIRECTORS, ... 259

BANK REFUSES TO HELP DISCOUNT-HOUSES, . . . 260
DOES NOT GET MORE GOLD WHEN NEEDED, . . . 261
USES ITS MONOPOLY TO INCREASE ITS PROFITS, . . 262
VICIOUS PRINCIPLES OF THE BANK ACT, ... 263
THE ACT UNWORKABLE BUT FOR NEW GOLD-MINES, . 264
AND THE CLEARING-SYSTEM, ... 265
EVILS OF PRESENT SYSTEM OF MONETARY RESTRICTION, 281 & 266
ABSURD ACTION OF THE GOVERNMENT WHEN BANK ACT SUSPENDED, ... 268
PARALLEL BETWEEN BANK ACTS AND THE OLD CORN-LAWS, ... 268 and 269

CHAPTER XVI.

THE CURRENCY, PAST AND PRESENT, . . . 270
OUR CURRENCY-SYSTEM A CHAOS, ... *ib.*
HOW THE BANK OF ENGLAND WAS FOUNDED, . . 272
THE BANK OF SCOTLAND, ... 273
EXCELLENT WORKING OF BANKING-FREEDOM IN SCOTLAND, 274
EVIL EFFECTS OF MONOPOLY IN ENGLAND, . . . 275
UNSOUNDNESS OF THE ENGLISH BANKING-CURRENCY, . 276
HOW THE GOVERNMENT ATTEMPTED TO REMEDY IT (1833), 277
SECOND ATTEMPT IN 1844, ... 278
NO CHECK ON THE MONOPOLY THUS ESTABLISHED, . . 279
WEAKNESS OF THE PROVINCIAL BANK-CIRCULATION OF ENGLAND, ... 280
GENERAL EFFECTS OF OUR PRESENT MONETARY SYSTEM, 281

CHAPTER XVII.

FOREIGN SYSTEMS OF BANKING, ... 285
FRANCE, ... *ib.*
BELGIUM, ... 290
HAMBURG, ... 291
THE UNITED STATES, ... *ib.*
SUMMARY OF THOSE VARIOUS SYSTEMS, ... 293

CHAPTER XVIII.

THE STATE AND THE CURRENCY, ... 295
STATE-ISSUES OF PAPER-MONEY, ... 296
EQUIVALENT TO FORCED LOANS, ... 297
SUSPENSION OF SPECIE-PAYMENTS IN 1797, . . . 298
DIFFERENCE BETWEEN STATE-ISSUES AND BANK-ISSUES, . 299
MR GLADSTONE ON STATE-ISSUES, ... 300
HIS STATEMENT CONSIDERED, ... *ib.*
HAS THE STATE A RIGHT TO PROFIT ON BANK-NOTES? . 302
WHAT THE STATE WOULD GAIN THE PUBLIC WOULD LOSE, 303
AND MUCH MORE, ... 304
VARIOUS FORMS IN WHICH A PAPER-CURRENCY CAN BE ESTABLISHED, ... 307
REQUISITES OF A PERFECT CURRENCY-SYSTEM, . . 308
A SINGLE BANK, OR PLURALITY OF ISSUE? . . . 309
A STATE-CURRENCY, ... 310
ITS LIABILITY TO EXCESS, ... 311
HOW IS IT TO BE ISSUED? 313
A STATE BANK, ... 314
OBJECTIONS TO IT, ... *ib.*
STATE-NOTES ISSUED BY THE BANKS, ... 316
UPON WHAT CONDITIONS? 317
OBSTACLES TO THE STATE UNDERTAKING TO SECURE THE CONVERTIBILITY OF THE NOTE-CURRENCY, . . . 320

CHAPTER XIX.

MONETARY REFORM, ... 325
GREATEST DEFECTS OF OUR PRESENT SYSTEM, . . . *ib.*
THE CHIEF ENDS TO BE ATTAINED, ... 326
SPECIAL OBJECT OF PAPER-MONEY, ... 328
PLANS PROPOSED FOR MAINTAINING THE MEASURE OF VALUE, ... 329
BY FIXING THE AMOUNT OF THE CURRENCY, . . . *ib.*
BY A FIXED BANK-RATE, ... 330

CIRCUMSTANCES WHICH AFFECT THE BANK-RATE, . . 333
THE OLD SYSTEM, ... 331 and 335
ALTERNATIVE MEASURES OF REFORM, ... 336
(1) AN INCONVERTIBLE STATE-CURRENCY, . . . 337
GENERAL PRINCIPLES OF SUCH A SYSTEM, . . . *ib.*
SUSPENSION OF SPECIE-PAYMENTS SOMETIMES ADVANTAGEOUS, ... 338
EFFECTS OF A SUSPENSION OF SPECIE-PAYMENTS, . . 339
PROPOSED PLANS FOR AN INCONVERTIBLE CURRENCY, . 341
A BETTER PLAN, ... 345
HOW IT WOULD WORK, ... 346
(2) A CONVERTIBLE BANKING-CURRENCY, ... 349
CONDITIONS OF ISSUE, ... 350

CHAPTER XX.

FREE TRADE IN BANKING, ... 353
THREE DIFFERENT MODES PROPOSED, ... 354
OUR PLAN DEVELOPED, ... 357
OBJECTIONS TO IT MET, ... 363
ADDITIONAL PROPOSALS, ... 372
AN ISSUE OF £1-NOTES CONSIDERED, ... 374
OTHER FEATURES OF THE NEW SYSTEM, ... 378
INFLUENCE OF NEW SYSTEM ON THE BANK-RATE, . . 382

CHAPTER XXI.

REFORM OF THE BANK OF ENGLAND, . . . 389
GENERAL POSITION OF THE BANK, ... 391
ITS NOTE-CIRCULATION, ... *ib.*
ITS DEPOSITS, ... 395
ITS LOANS AND DISCOUNTS, ... 398
COMPARISON WITH OTHER BANKS, ... 399
WITH BANK OF FRANCE, ... 400
FORM IN WHICH ITS ASSETS ARE KEPT, ... 404
GOVERNMENT SECURITIES IN ISSUE DEPARTMENT, . . *ib.*
GOVERNMENT SECURITIES IN BANKING DEPARTMENT, . 408

SPECIE IN ISSUE DEPARTMENT, ... 412
SEVEN MILLIONS NULLIFIED BY BANK ACT, . . . 413
EVIL EFFECTS OF THIS ARRANGEMENT, ... 414
RECAPITULATION, ... 416
GENERAL EFFECTS OF PRESENT SYSTEM, ... *ib.*
THE NEW SYSTEM, ... 417
THE GOVERNMENT DEBT TO THE BANK, ... 431

CHAPTER XXII.

BANKING-PROFITS UNDER THE NEW SYSTEM, . 435
THE BANK OF ENGLAND, ... 436
PRELIMINARY CHANGES, ... 439
SOURCES OF LOSS, ... 441
EFFECTS OF THE BANK'S LENDING-POWER, . . . 445
SOURCES OF GAIN, ... 450
THE SCOTCH BANKS, ... 455
THE IRISH BANKS, ... 457
THE ENGLISH PROVINCIAL BANKS OF ISSUE, . . . 460
THE PRESENT NON-ISSUING BANKS, ... 461

CHAPTER XXIII.

AN INTERNATIONAL MONETARY SYSTEM, . . 464

CHAPTER XXIV.

SUNK CAPITAL, ... 499

CHAPTER XXV.

STATE FINANCE, ... 509
GENERAL EFFECTS OF TAXATION, ... 512
THE USE OF A GOVERNMENT, ... 513
FINANCIAL ADVANTAGE OF CHEAP GOVERNMENT, . . 515
TAXATION ILLUSTRATED, ... *ib.*
TAXATION EXPENDED ABROAD, ... 517

INCIDENCE OF TAXATION AND EXPENDITURE, . . . 521
THE NATIONAL DEBT, ... 523
A SINKING-FUND, ... 525
CREATION OF A NATIONAL DEBT, ... 529
IS IT AN ECONOMY TO PAY OFF THE DEBT? . . . 530
QUESTION AFFECTED BY THE RATE OF INTEREST, . . 536
THE QUESTION OF THE FUTURE, ... 540
POLITICAL CONSIDERATIONS, ... 541
THE QUESTION AS IT AFFECTS FISCAL REFORMS, . . 542

CHAPTER XXVI.

THE STATE AND THE RAILWAYS, ... 544
MR CRAWFORD'S PLAN, ... 551
OTHER PLANS, ... 560
GENERAL OBJECTIONS, ... 562

CHAPTER XXVII.

RAILWAY FINANCE, ... 563
FAULTS IN THE PAST, ... 566
PRESENT DIFFICULTIES, ... 572
REMEDIES, ... 577
RAILWAY-SECURITIES COMPANIES, ... 579
IMPROVED FORM OF BORROWING, ... 586
IMPROVED FORM OF ACCOUNTS, ... 588
A RESERVE-FUND, ... 590
WORKING-EXPENSES, ... 592
CHARGES TO CAPITAL, ... 593
REQUIREMENT FOR STEADY DIVIDENDS, ... 598
AUDIT OF THE ACCOUNTS, ... 602
INSOLVENT RAILWAYS, ... 604
THE FUTURE OF RAILWAYS, ... 609

CHAPTER XXVIII.

MUNICIPAL FINANCE, ... 616

CHAPTER XXIX.

LAND FINANCE, ... 622

CHAPTER XXX.

THE STATE, THE POOR, AND THE COUNTRY, . . 637

APPENDIX.

ANNUAL ABSORPTION OF SPECIE, ... 679
STATISTICS OF THE CRISIS OF 1866, ... 680
COST OF NOTE-ISSUES, ... 691
A RAILWAY RESERVE-FUND, ... 692
THE GAS AND WATER SUPPLY OF LONDON, ... 695

THE

SCIENCE OF FINANCE

OUR INVISIBLE CAPITAL

THERE are marvels in common life which escape attention, simply from our familiarity with their external appearance. Travellers have often been struck by the insensibility of the inhabitants of a picturesque country to the natural beauties which are daily before their eyes. And a like insensibility characterises those who inhabit an unattractive scenery. Familiarity does not necessarily beget contempt, but it blunts the habits of perception. If the Scottish mountaineer is unsensitive to the sublime and picturesque scenery which surrounds him, so is the peasant of the Landes of France to the dreary monotony of his district; so also is the wandering Arab to the level waste of far-spreading sands, only enlivened by the illusions of the mirage. In order to appreciate our condition or surroundings, we must also know the opposite. It is proverbial that one only knows the value of what he

possesses, by the loss of it. A stranger to our scenery or condition of life can better than ourselves appreciate its peculiar features. We remember the impression produced by a first visit to Paris after the renovation of that city by the genius of the present Emperor. Sauntering through the environs of the Tuileries and the Louvre, viewing the Place Vendôme, the Place de la Concorde, the Champs Elysées, and the Bois de Boulogne, the scene seemed immeasurably to surpass anything of the kind to be met with in England. And perhaps rightly. Yet, on returning to London, when driving home from the railway station, in full view of the Parks and Piccadilly and Buckingham Palace, we felt we had been rather hasty in our judgment. We saw more of the grandeur of London than we had done for years; and were made to think with respect of the impressions first produced upon us by that scene. We were recalled to our first impressions, and felt that they were the right ones. We became conscious that a residence of years in the English metropolis had blunted our sensibility to its grand and peculiar features.

It is the same in all departments of life. The man of science, who in his novitiate has great difficulty in understanding the strange terminology, soon comes to use the hard terms of chemistry or other sciences as if they were equally familiar to all. The preacher in like manner uses terms which are shorthand expressions for abstruse confessions of faith, which perhaps he fully understands, but which to the yearning human hearts of his congregation are but dry bones,—phrases hard to

be understood, and frequently unintelligible when the listener most anxiously and earnestly seeks to grasp their meaning, and lay them as a comfort to his troubled heart. Thus an outsider is often a better observer of peculiarities, a better appreciator of anomalies and intellectual difficulties, than they to whom those peculiarities, whether of scenery or of social condition, have become familiar.

Lately we took a friend from the country to see the famous City of London, and especially that "City of Gold" which forms its inner heart. We showed to him the Royal Exchange, the Stock Exchange, the Discount-houses, and other great marts of buying and selling. And the whole affair struck him as strange. He said, "I see no buying and selling." The actual and sole business of the place, which was going on under his eyes, was invisible to him. He was not blind,—but in truth there was nothing like ordinary buying and selling to be seen. Accustomed to the great agricultural fairs in Scotland, where dealers come from all quarters, each with bundles of notes or sometimes rouleaus of sovereigns, he marvelled and questioned how buying and selling could be carried on without an interchange of money. And when we told him of the immense sums which were changing hands under his eyes, and which do so daily in these London marts, his wonder, if not his scepticism, was still further increased. "Where is the money?" he asked again. "If money is changing hands, where is it?" And when we replied that we did not say that Money was changing hands, but that Capital was, his look and silence assured us

that we need not, in that place at least, continue the discussion.

"Where is the money?" Although the question may appear ridiculous to City men, it is a natural and reasonable one. Our friend is a man of excellent intelligence; we would as soon discuss a knotty question of any kind with him as with the most knowing members of the Stock Exchange. Only he had not, like them, from familiarity become unsensitive to the real marvels of the City of Gold. Nevertheless, he too had become unsensitive, in his own branch of commercial exchange. He forgot that to uncivilised communities, to men who deal only in barter—and the system of barter is not wholly exploded even in Europe—the ongoings at a Scottish fair would be as surprising as those of the City were to him. They would be as much astonished at sensible men giving away their sheep and cattle for bits of paper or of metal, as he at sales where no *money* is given at all.

In point of fact, on ordinary days (*i.e.*, not settling days) in the City of Gold—the great mart of financial and commercial exchanges—nothing seems to change hands at all. But let us follow the men of the Royal Exchange and Stock Exchange—the merchants and stock-brokers—to their offices, and what do we see? Payment for the stock or goods is made in bits of paper called Cheques, ranging in value from £5 to thousands of pounds sterling; or, as on the Royal Exchange, by bits of paper called Bills—which are promises to pay a certain amount of money at the expiry of a stated period. But look or inquire further, and see what the

recipient of these bits of paper does with them. If payment is made by bill, the recipient does not lie out of his money for three or four months—the ordinary term of commercial bills. He can employ the sum profitably in his business: so he takes the bill to a discount-house—some of which are among the largest and wealthiest establishments in the City, established for the sole purpose of dealing in, or cashing, commercial bills—and receives at once the amount promised to be paid, *minus* the interest for the three or four months which must elapse before the bill becomes due. And how does he receive the amount? In money? No: but in the form of a cheque—*i. e.*, an order on a particular bank to pay the amount in money. Well, follow him and see what he does with this cheque. Does he take from the bank the amount in money? Very seldom. He goes to his own bank, and, handing the cheque across the counter, orders it to be placed to his account,—to be drawn out afterwards in portions as he may require. The amount represented by the cheque then becomes part of the "deposits" of the bank,—part of the reserve-wealth of individuals intrusted to the keeping of the bank, and which the bank undertakes to repay in the form of specie on demand.

But what are those "deposits"? As we have seen in the case just described, they are not necessarily, nor are they generally, paid into bank in the form of money:* neither do they exist in the form of money. Banking-deposits exist mainly in the form of commercial bills,

* To show how very small an amount of banking-deposits are made in the form of money, we give the following statement, made by Sir

Government securities, &c., possessing real value, but without any corresponding amount of money in which they can be paid. The deposits in the banks of the United Kingdom amount to about four hundred millions sterling; whereas the total amount of money, whether in specie or in notes, held by all the banks seldom exceeds (if we deduct the gold locked up as a basis for the note-issues) twenty millions.* Here, then, is a strange matter. The banks promise to pay, and are liable to pay, £400,000,000 in money (not to say specie) on demand, yet the Money, whether coin or notes, which is available for the payment of these deposits is barely one-twentieth part! How is this?

It is a strange matter truly: yet strange as it is, the whole prosperity of the country depends upon the successful working of this peculiar arrangement. The

John Lubbock before the Statistical Society in June 1865, in which he analysed a sum of 19 millions paid into his bank by his customers:—

Cheques and bills, ...	£18,395,000	or 97 per cent
Bank of England notes, . . .	408,000	
Country notes, ...	79,000	3 ,,
Coin, ...	118,000	

From which statement it appears that only 3 per cent of banking-deposits are paid-in in the form of money—*i.e.*, notes and coin together, —and little more than ½ per cent in specie.

* The Bank of England, on the average, holds about 15 millions of specie, of which amount about 7½ millions are locked up in the Issue Department as security for its notes,—leaving 7½ millions to meet the demands of its depositors. The Irish banks hold about 2 millions of specie available in payment of their deposits; and the Scotch banks hold about £650,000 of specie, exclusive of the amount (upwards of two millions) which they are compelled to keep locked up as security for their note-issues. Add to this (say) 10 millions of coin and Bank of England notes held by the English banks, exclusive of the Bank of England, and we get 20 millions as the total amount of Money in the banks of the United Kingdom available to meet their liability to pay their 400 millions of deposits.

City of Gold—that city within a city, that inner heart of busy London—is the material capital of this great country, and every fluctuation in its condition affects the whole wealth and industry of the nation. And yet this great financial emporium, where the wealth and trade of the country are centralised, is itself dependent for all its power upon an Invisible Capital, which is the unseen motive power of all its transactions. This invisible capital is the life-blood of the place. Powerful as the electric currents, it is equally viewless. Stand like a dictator in the City of Gold, and order to be brought forth all its stores of money, whether gold or bank-notes, and the amount when presented would be totally insignificant compared with the actual wealth of the place and the amount of business carried on. The banking-deposits alone are twenty times greater than there is money to represent. And the imagination is baffled to conceive the amount of property which is constantly changing hands on the Stock Exchange, Royal Exchange, and Mincing Lane, without the intervention of money at all.

The accumulation of reserve-wealth, as witnessed at the present day, is really a singular thing. It is, perhaps, the greatest feat and marvel which Civilisation has produced. Yet it must not be thought that the process has reached its fullest development. The world ever moves on: material civilisation ever progresses. The wisdom of one age becomes a folly in subsequent generations. It is curious and interesting to mark the successive steps by which the accumulation of the reserve-wealth of individuals has reached its present

development: it is also eminently instructive. It is only by considering the progress of past times in this branch of civilisation, in this department of science, that we can clearly understand our present position, and become alive to the necessities which may ere long impel us to a further advance, and to the principles which ought to regulate our progress.

What, then, in brief, has been our past progress in monetary science—in the economy of capital—in the means by which Capital has been so potently brought to the support of Trade? By what means have we succeeded (1) in storing the ever-increasing reserve-wealth of individuals, and (2) in making this wealth adequate to the support of an ever-expanding Trade?

We need not dwell upon the Origin of Capital, upon which some political economists delight to exercise their theorising ingenuity. We desire to adhere to facts of practical moment at the present day. But in order to enable the reader to judge of the present position of monetary science, and of our existing monetary system, it is indispensable at the outset to exhibit the various processes by which the Accumulation of Capital —the storing of reserve-wealth—has been carried on. In proportion as wealth has increased, new methods of storing it in a convenient form have been devised. This is a necessity to which the whole past history of civilisation bears witness; and it is a necessity which in the present day, despite the enormous supplies of the precious metals from California and Australia, begins to be felt anew.

Judging by our present social arrangements, the

origin of Capital would be thus:—A man, either by his superior skill in producing, or by his greater economy in consuming, would acquire more goods than he used. The surplus he would give to others who required it, on their giving to him in exchange some other kind of property, which he would lay-by as reserved wealth. As a matter of fact, however, the origin of capital, the accumulation of wealth not needed for its owner's consumption, took place otherwise. Instead of superior skill in producing, or greater economy in using, it was the greater personal power of certain individuals over the rest of the community which gave them the means of acquiring capital, —by exacting property, willingly or unwillingly, from others. For example: a man famous in war, or otherwise superior to his fellows, became the chief of his people, or one of the chiefs or elders—who, generally by free consent, obtained from the community a portion of their annual produce. A chief or king, in virtue of his office, was supported by payments in kind: and in this way, he acquired a greater quantity of goods than he himself could consume. The surplus was reserve-wealth, which he kept to meet emergencies, or which he parted with in exchange for labour, or for commodities of a less perishable nature and lesser bulk than those which he held, and therefore more suitable for storing.

In order that goods be readily exchangeable, they must be such as there is always a demand for. In the earliest times this was Food,—grain or cattle. By-and-by, especially in Eastern countries, apparel also

came into vogue as a form of accumulated wealth. In the East, where the mode of dress is not, like that of modern Europe, fitted to the shape of each person—like our tight coats and trousers—but consists of robes which fit all persons alike, the great and wealthy men turned a portion of their surplus goods into robes and other articles of apparel. Thus a king, or wealthy man, kept large flocks of sheep and oxen, and stores of grain, and also so many dresses — which were likewise in demand, and therefore were exchangeable property. But food is liable to corruption,—herds of cattle die in due course,— robes also are doomed to decay, through moths and other destructive agencies. But the precious metals next, and to some extent simultaneously, rose into esteem as prized ornaments. They formed articles of apparel which, from their beauty, were prized by all; and moreover, as they were not liable to corruption, and could be easily carried about, they were soon recognised as the kind of goods most suitable for storing and accumulating,—as the best form in which individuals could keep their surplus wealth. So that, when a man possessed more goods of a perishable kind than he required, he sold these to others in return for gold and silver, which were not subject to decay, and which were exchangeable for other articles.

Next, as all men valued these metals, kings began to collect their revenue in that form. They coined the metal, and made it receivable as tribute or taxes. This fully established the exchangeable value of the precious metals. It created a new demand for them:

it rendered them indispensable in a department of national life where they had not previously been required; thenceforth, all men needed them every year to pay the king's dues. Thus they became a circulating medium. A man who had more oxen or grain than he needed for his own use, sold these commodities to others, receiving coins in return,—which coins he could store for ever, which were useful to pay taxes, and, when he so needed, to purchase the labour or productions of others.

The accumulation of Capital thus led to the origin of Money, as a means of storing and employing it. But the invention of money by no means put an end to payments in kind and the process of barter. It only supplemented them. Exchanges of goods for goods went on simultaneously. Even in England until the reign of Edward I., the taxes were paid in kind to a large extent, if not entirely: and to a much later date, military or other personal service to the State was accepted in lieu of taxes of any kind. The dues to lords of the manor and to monasteries used always to be paid in kind,—so many oxen, or fowls, fish, grain, &c. Rents also were paid in this way. But steadily the use of the precious metals as money extended. As mercantile operations widened, so did the use of coins. Cattle and goods could not be sent great distances—could not be transmitted from country to country in payments. Moreover, as the wants of men multiplied, instead of taking any particular kind of goods in payment of their services, they preferred payment in money (coins), which they could keep,

or convert into any kind of goods which they wanted, and in such portions as they required. Instead of having to sell an ox when they only wanted to buy one sheep or a pair of fowls, they bought what they required by giving the exact value in coins. In this way money (metallic money) came into general use as the medium of exchange—of paying debts and making purchases. Hence it became almost the only form in which men kept their reserve of wealth. Traders and others, of course, kept the greater part of their wealth in the form of goods,—for that was simply carrying on their business. But the purely reserve-wealth — the wealth acquired by individuals, but not used by themselves—was kept in the form of metallic money. This was the third stage in the accumulation of Capital.

Ere long another step came. Men who held a large stock of specie, especially in those comparatively unsettled times, wished to place it in safer quarters than their own dwellings. They deposited it with certain parties—with goldsmiths, or under the guardianship of the State, or in banks of deposit — for better security. This was the origin of Banking; and out of it arose a great economy. None of the previous stages had effected any economy of capital. When the precious metals were stored instead of grain or goods, or when coins were stored instead of bullion, there was no economy in either arrangement, only it was a more convenient one. But with the establishment of Banking began that system of economising capital which has ever since been progressing. At the outset, more than a century and a half ago, it

was found that, of the money deposited in banks, not more than one-fifth was liable to be called for, at any one time, by the owners. A million sterling being deposited, if a bank kept on hand £200,000, that was enough to meet the current demands upon it. So that a banker could lend out four-fifths of the silver intrusted to his keeping, and get interest on that sum, and yet be always able to meet the demands made upon him by depositors. In other words, the owners of the capital could always get it when wanted, while, nevertheless, the greater part of it was lent to others. Thus, although the quantity of capital in a country remained the same, its potency was immensely increased. And practically, this is the same thing as if an actual addition were made to the amount of capital.

To show the first effects of Banking, let us take the following case:—Suppose there are twenty millions of gold and silver coins in a country, of which ten millions are hoarded (*i.e.*, kept in hand by individuals as reserve-wealth), and the remainder is absorbed in the active circulation of the country. Banks, when established, would receive as deposits the ten millions of coin previously hoarded, but need not keep on hand more than one or two millions,—giving back to the public the remaining eight or nine millions, either to be absorbed in the active circulation, or to be re-deposited in bank. In this way these ten millions previously hoarded would either, if kept in bank, allow of the reserve-wealth of individuals (as kept in the form of banking-deposits) to increase from 10 to 50 or 70 mil-

lions; or else, if the specie were needed as currency, would allow of the active circulation increasing from 10 to 18 or 19 millions,—the banks being able to put into circulation more than four-fifths of the 10 millions deposited with them.

It was the vast addition to the precious metals, arising from the discovery of the New World, which gradually led to the abandonment of the old system of barter and payments in kind. Without these new supplies of gold and silver, no such change was practicable. However much men might have desired to adopt money-payments in lieu of payments in kind, they could not have done so, because the supply of specie was totally inadequate for such a change. It was the great supplies from the New World which enabled this change to be accomplished. But by-and-by, the increase of population and of trade began to multiply monetary transactions in greater ratio than the yearly produce of the mines added to the stock of specie. The world again began to be pinched for want of the precious metals. And as no new discovery of mines took place, man had to remedy the defect for himself. Which he did—first, by the establishment of banks; and, secondly, as a natural consequence of banks, by the adoption of Paper-money.

This was the next great step. Trade and all kinds of business were increasing rapidly; so also—it may be said, in similar proportion—was the reserve-wealth of the country. There was thus, as there is at all times, a double requirement for specie — a twofold process of absorption of the precious metals. With the lapse

of every year, more coin was needed (1) to carry on the increase of buying and selling and all kinds of business; (2) more coin also was needed to store the increased profits which flowed from this increase of business. Banking multiplied the power, by economising the use, of the precious metals (or rather of such portion of them as was kept as reserve-wealth). Banking economised greatly that portion of the precious metals which was employed in the storing of capital, —the specie deposited in bank by one man being immediately lent out to another; but (apart from the later system of notes and cheques) banking had no effect in economising the specie used as currency. Paper-money, however, produced an economy in both departments. It took the place of the precious metals as a means of representing banking deposits, and also as employed in the currency. It supplemented the use of specie. It did not throw any of the metallic money out of use,—on the contrary, the stock of specie in this country continued to augment: but the increase in the stock of specie was not equal to the simultaneous increase in the monetary requirements of the public, —and it was this vacuum, this difference between the supply of specie and the requirement for currency, which paper-money filled up.

The adoption of paper-money, in fact, was equivalent in its effects to an increased supply of the precious metals. It was as a substitute for and supplement of metallic money that bank-notes were originally employed: and that is their sole use. It was to permit the expansion of trade and industry without import-

ing specie in the large quantities requisite to meet the ever-increasing monetary wants of the community. Also, it was to compensate the temporary withdrawal or diminution of our ordinary stock of specie, which takes place in times of war, bad harvests, &c. The Bank of England was established for the purpose of supplying with its notes the place of specie, during a time of war — in order that the specie might be exported. And the result was, that the trade and industry of this country obtained free scope to expand, instead of being prematurely checked by the want of an adequate supply of money to carry it on. Trade, it is needless to say, cannot increase without a corresponding increase in the means of carrying it on. Whatever number of carriages and horses a carrier may buy, unless he have a proportionate number of wheels he cannot transport a single hundredweight more than before. In like manner, although a country produce more goods for foreign trade, and although there be an equal increase in the demand for those goods abroad, an increase of trade is impossible unless the means of paying the trade-balances be commensurately increased. For example, but for the new mines of California and Australia, our trade with the East could not have increased as it has done; for the balance of trade with the East has always been against us, which balance has to be paid in specie,—and we could not possibly have spared so much specie but for the discovery of the new mines, which enabled Europe to fill up with gold the vacuum produced by the export of its silver-money to the East.

If you give a man the means of getting a certain amount of specie or other goods whenever he wishes to have it, it is as good to him as if he had the article itself. This is the principle of Paper-money. It was also the principle upon which metallic money itself was at first received in payment. When a man gave away his grain or cattle in exchange for coins, he obtained a means of re-acquiring an equal quantity of grain or cattle whenever he wished, — and that was all he wanted. The coins, indeed, were not a means of getting back so many oxen from the man to whom he gave his, but from the community at large. The acknowledgment of debt was thus virtually converted from a bond upon a single individual, to a bond upon the community at large. A bond which all alike recognised. This was the great good of Money.

Paper-money grew into use in various ways:—

(1.) The Jews, ever liable to persecution, adopted a system of drafts or written orders upon one another, which each agreed to honour and pay to the person named in the draft. In this way Value was transmitted from country to country much more cheaply than if silver had been sent; also much more safely, seeing that the bonds were of no use if they fell into improper hands.

(2.) The Bank of Venice. It was a bank of deposit, —a place where people deposited their gold and silver, under the guardianship of the State, and received receipts for the amount, payable in coin on demand. As these receipts were convertible into silver on demand, they were held as valid as silver itself; and

hence they became currency—a means of making purchases or of paying debts, just as if they were silver-money. By-and-by the State, being in want of money, gradually abstracted the silver from the bank, unknown to the public. But when at length the fact became known that the silver was all gone, the receipts of the bank continued to circulate as before. Why? Because those receipts, although no longer representing a certain amount of silver, represented a debt due to the holder by the State, and also were receivable in payment of taxes. The best security an individual can have is the security of the State,—seeing not only that it is generally the safest, but also that the State paper-money, or vouchers of the debt, is always a means of paying the yearly taxation or dues to the State.

(3.) The Bank of England. The Government was in want of money to carry on the war on the Continent. It had to feed and pay its army. Now, it was cheaper to send money abroad to buy food for the troops than to send the food from England; moreover, there were not the means of transport. To meet these monetary wants of the Government, the Bank of England was established. A Company raised £1,200,000 in specie (the only form of money then in use), and lent this sum to Government, on condition that the Company was paid interest for the loan, and at the same time was allowed to issue notes to the amount of the loan—which indeed was needed, to supply the vacuum caused by the abstraction of the specie sent abroad. The security being good, the notes being receivable in payment of taxes, and the Bank

also engaging to give specie for them when required, this paper-money circulated freely; and the grand basis was laid upon which has grown up our subsequent prosperity. A great service was rendered to the State, and a great economy to the country. The Bank made a profit by it,—the State got the money it so sorely needed,—and the people obtained a currency which they took as readily as silver, and which possessed the invaluable power of expanding with the growth and monetary requirements of the country. These notes, too, did not owe their circulation in any degree to compulsion. They were not made legal tender,—any person was at liberty to decline receiving them if he chose. The introduction of paper-money into this country owed all its success to the goodness of the security and the soundness of the project.

A temporary want of money on the part of Governments has led to similar or analogous measures in other countries; paper-money being issued as vouchers of debts due by the State—or, as in the case of the French assignats, on security of Crown property. It was in such forms as these that paper-money was first adopted in America, Russia, Austria, and other countries.

As long as the only form of money was specie, it is obvious that no increase in the currency of a country could take place without an increase of the precious metals. The amount of these metals needed for the ordinary transactions of the country would not diminish,—on the contrary, it ever augments, in consequence of the steady increase of those transactions.

So that, as long as nothing but specie passed for money, each progressive country would require an increasing amount of the precious metals to carry on even its internal business, payment of taxes included. And still more gold and silver would be required if (as always happens) the accumulated profits and reserve-wealth of individuals were likewise increasing. More coin cannot be stored, whether in bank or in its owner's coffers, unless more bullion is brought into the country. And bullion can only come in as a consequence of the exports exceeding the imports. Hence the old Mercantile System, which aimed at keeping the exports always in excess of the imports, was quite right in its day.

As long as specie was the only recognised kind of money, and the chief form in which reserve-wealth was stored, it was advantageous for a progressive country to keep its exports in excess of its imports: otherwise it would have no means of increasing its currency or of suitably storing the capital which it was accumulating. Take the Bank of Venice for example. Venice was at that time an eminently progressive State. It made profits on its foreign trade; and these profits were accompanied, and represented, by an increase of the imports of the precious metals. This surplus of bullion (minus some portion of it required by the increasing monetary wants of the community) was deposited in the bank,—the bank's stock of bullion increasing with every increase of the capital or reserve-wealth of the country. But without such an increase in the imports of the precious metals, no increase of

banking-deposits could in those times be made; and men would require to keep their reserve of wealth (as of old) in the shape of corn or cattle, or some other perishable and inconvenient form. Hence the Mercantile System was the right one for those times. No system which has largely prevailed was ever devoid of foundation in reason. Yet such is the narrowness of human intellect, that what is right for us we think must have been right in previous times. A great though natural mistake. As long as specie was the only kind of currency, and the chief form in which reserve-wealth was stored, the Mercantile System was the right one.

It was the introduction of paper-money which upset the Mercantile System in this country. Not immediately, it is true; for men naturally proceed upon old principles until the new ones have taken a great development. But it was paper-money, in the form of banking-currency, which upset the old system,—the earlier form of which was to prohibit the export of bullion—the later, to keep exports always in excess of imports.

But two other steps were needed, and were accomplished, before our monetary system attained its present development. The first of these was the Cheque-system,—the making payment by orders upon banks, instead of by coin or notes. The origin of this system dates back nearly a century: but for a long time the great importance of the change was not recognised. It was a new and most valuable onward step in the process of economising capital. The second and culminat-

ing stage of the process—and one to which the cheque-system naturally led—was the establishment of the Clearing-House: an office to which each bank sends the cheques upon other banks which have been paid into it, and where a balance of these transactions is struck,—the banks now settling the amount by cheques upon the Bank of England.

Let us now recapitulate the various stages in the economy of capital which, in succession, have been accomplished in this country.

I. *Banking.*—When banking was first introduced in this country, the only recognised form of money was metallic money—gold and silver. The economy of capital, in the form of specie, which was effected by banking, took place as follows: A bank which received a million sterling of specie in deposit from its customers, found that only a small proportion of this amount required to be kept on hand to meet the demands or requirements of the depositors. Hence the remainder of the amount deposited in bank can be lent out. This the banks do by discounting commercial bills (payable on the average at three months' date), or in advances upon other good and negotiable securities—bonds and stock of various kinds. The economy thus effected is very great. Ninety-five per cent of the money deposited in bank is put into circulation again, in the shape of loans; instead of the whole amount lying unused in the hands of its owners, as used to be the case before the banking-system was established. Thus banking, even if the currency were purely metallic money, would economise specie to the

extent of four-fifths, or, as in present times, more than nine-tenths.* This would be the effects of banking quite independent of the use of bank-notes — paper-money.

II. *Bank-Notes.* — But, with the establishment of banks in this country, there simultaneously arose the use of paper-money. The credit of the banks being good, the public took their notes (promises to pay specie on demand) just as if they were specie. As we have said, when a man can get an article whenever he wants it, it is practically the same as if he actually had the article. It was on this principle that bank-notes were introduced, and found ready favour with the community. It was found by experience at the very outset—*i.e.*, 170 years ago—that of the notes put into circulation, not more than one-fifth, on the average, were brought to the bank to be cashed,—of the promises to pay in specie, issued by the banks, only in one case out of five was payment in specie asked for. The notes were recognised as good money, and circulated freely among the community.

Mark the economy thus effected. Banks, without the employment of paper-money, could (in those times)

* Now that the credit of our banking-system has been well established, and especially owing to the growth of large banks, the reserve in cash which a bank has to keep on hand is very much smaller in proportion to its liabilities than was necessary in early times. For example, in the case of the London and Westminster Bank, it was stated by the chairman that during the year 1865 the amount of the deposits fluctuated only to the extent of one million sterling—the maximum being 19½ millions, and the minimum 18½ millions. Thus the utmost demand upon the banking-reserve of the establishment could not possibly have exceeded one-eighteenth part of the deposits. But as a great part of the variation in the Bank's deposits during the year was

lend, and so put into circulation again, four-fifths of the capital intrusted to their keeping. They needed to keep on hand only one-fifth of the specie deposited with them. And, when paper-money came into play, they found that this reserve of specie would suffice to support a note-circulation of five times the amount. For example, if a bank received deposits in specie to the amount of £1,000,000, £200,000 was sufficient to keep in hand to meet the ordinary requirements of the depositors. But after paper-money came into use, it was found that, in ordinary times, in four cases out of five the depositors were willing to take repayment of their deposits in the notes of the bank. So that this reserve of £200,000 in specie was practically increased fivefold—became a million sterling, of which £800,000 was in bank-notes. Nowadays, in ordinary times no notes are cashed at all, save as a means of getting small change, — which demand for coin is occasioned by the fact that no notes are allowed to be issued in England for less than £5; and in Scotland, where £1 notes are in use, no demand even of this kind takes place.

occasioned by an *increase* in their amount, hardly any portion of the reserve was called into play at all. In fact, as the banking-deposits of the country are increasing every year, the amount of money withdrawn from any good bank by its customers each day is balanced, or more than balanced, by the amount simultaneously paid in by other customers: so that actually, in such cases, the bank does not in ordinary times require to keep any cash in hand at all. This is the fact,— and simply as a fact we mention it. But the first element in banking is perfect security: and we need not say that it is indispensable that every bank should keep a reserve amply sufficient, not merely for its ordinary requirements, but to meet the demands upon it even in the most exceptional times.

III. *Cheques.* — The tendency, and actual result, of the use of cheques is to lessen the amount of money (whether notes or coin) which a bank has to keep on hand to meet the wants of its depositors. Previous to the use of cheques, every man who had to make a payment had to go to his bank and draw out the amount in notes or coin. But now, instead of drawing out money from the bank, he gives a cheque—an order on his bank to pay the amount. If the person who receives the cheque deals with the bank upon which the cheque is drawn, no money changes hands at all: the amount is simply transferred in the bank's books from one depositor's credit to another's. This case, of course, does not very often happen. In a majority of cases, the person who receives the cheque deals with a different bank from that upon which the cheque is drawn. In such a case, he pays the cheque into his own bank, and that bank receives the amount in money from the bank upon which the cheque is drawn. Or rather, as thousands of cheques are drawn every day—so many upon one bank, so many upon another,—it is only the balance of these cheque-transactions which requires to be transferred in money from one bank to another. This of itself is a great economy: for (1) not only is no money needed by a bank's customers (we may say the public) in making their payments, and consequently no money is withdrawn for this purpose from the banks at all: but (2) only the balance of these transactions requires to be transferred in money from one bank to another. The amount of Money (coin or notes) in the banks of the country is totally

unaffected by these cheque-transactions,—the requirement for money remains the same whether these transactions amount to thousands of pounds or to many millions: the only result is the transfer of the balance of these transactions, in the form of Money, from one bank to another.

The economy thus effected by the cheque-system is very great. The amount of money employed by the public is trifling compared with what would be needed if cheques were not used, and if every payment had to be made by withdrawing the amount in money from the banks. In fact, if the payments now made by means of cheques had to be made in money, all the notes and coin not only kept on hand in the banks, but also circulating in the country, would be totally inadequate for the purpose.

IV. *The Clearing-House.* — The economy of the cheque-system *per se* consisted in allowing the innumerable daily payments of the community to be carried on without any withdrawal of money from the banks. The next and culminating step in the process was to allow of the payments among the banks themselves to be likewise effected without the use of money. This has been admirably accomplished by means of the Clearing-House. This is an establishment to which each bank sends the cheques upon other banks which have been paid-in by its customers, and where a balance of these cheque-transactions is struck for each bank with each of the others. This system was adopted at first simply as a convenience for the banks: instead of each bank sending round to

settle with each of its neighbours, both time and trouble were saved by the representatives of the banks meeting at a certain place and at a certain hour to settle the business. This arrangement, though devised at first merely for the convenience of the banks, led to a further economy of capital in the form of money. The balances due to or by each bank being ascertained at the Clearing-House, it was agreed that these balances should not be paid in money, but by cheques on the Bank of England. All the banks in London, and some of the provincial banks, keep an account at the Bank of England. In fact, a large portion of the deposits in the Bank of England belong, not to private customers or to the State, but to the other banks. And the settlement at the Clearing-House is effected by each indebted bank giving to the others a draft, or cheque, upon the deposits which it keeps in the Bank of England. Hence the business of the Clearing-House—the balance of all the cheque-transactions—is settled without the use of money at all, simply by a transference of a certain amount from the credit of one bank to that of another.*

* To show approximately the proportion of banking-transactions which are settled through the Clearing-House, Sir John Lubbock (in a paper read before the Statistical Society in June 1865) made the following analysis of 23 millions sterling which passed through his bank in a few days :—

Amount settled through Clearing-House, . .	£16,346,000	or 70 p. c.
Cheques and bills, not passed thro' Clearing-House,	5,394,000	,, 24 ,,
Bank-notes, ...	1,216,000	,, 6 ,,
Coin, ...	139,000	
	£23,095,000	

From this statement it appears that 70 per cent of banking-transac-

By this means payments to the enormous amount of about fifteen millions sterling take place daily throughout the country without the use of a single note or coin.* No money is withdrawn from the banks to make these payments; neither does any money change hands among the banks themselves. The only result of these millions of daily payments made by cheques is, that the clerks in the Bank of England take their ledgers and write off a trifling amount from one bank's credit, and place it to the credit of another. A few minutes' work with the bank-books in Threadneedle Street settles the whole business. The *means* by which this settlement is made are a few lines of writing—a few entries made by a clerk,—that is all. And as to *what* is transferred there is little to show. It has a name—it is called Capital; and it has real value; but it has no bodily form like most other kinds of property. It appears in the mass a mere fiction; nevertheless it always takes a bodily form when it is wanted. The handful of Money in the banks suffices to represent the whole amount of Wealth intrusted to their keeping, because only a small portion of that wealth requires to be converted into money at any one time. Just as Fortunatus's

tions are settled through the Clearing-House, and consequently without the use of money. Of the remainder, also, 24 per cent are settled without the use of money, by means of cheques and bills; nearly $5\frac{1}{3}$ per cent are settled in bank-notes, and little more than $\frac{1}{2}$ per cent in coin.

* Mr Hankey ('On Banking,' p. 101) states that the transactions settled through the Clearing-House last year amounted to 4588 millions sterling: giving an average of nearly fifteen millions a-day! This, we presume, is apart from the economy effected by the recently-established Country Clearing-House. The Scotch banks, also, have a clearing-system of their own.

purse, which never became empty, enabled him, though there were but a few coins in it, to spend unlimited sums, so the amount of Money in the banks, comparatively small as it is, nevertheless suffices to utilise the whole amount of their deposits. Banking-deposits, in truth—the mobilised reserve-wealth of individuals—are like a score of viewless or disembodied spirits who have only one body amongst them Give them time, and all of them, each incarnating himself in turn, will appear before you. But it is impossible they can all appear at once. As there is only one body for the score of them, nineteen out of the twenty must always be invisible. So is it with the wealth deposited in banks. By a marvellous process, or rather by a succession of processes, we have carried financial economy so far that nineteen-twentieths of our reserve-wealth (as represented by banking-deposits) has no existence in the shape of money at all; and yet it can all be utilised.

In the storing of reserve-wealth, the first improvement was to transmute property so kept from a perishable form (corn, cattle, &c.) to an imperishable one, by the use of the precious metals in the form of bullion. The second process was to convert this bullion into a more commodious and negotiable form by the adoption of metallic money or coins. The third step was banking, which greatly economised the use of specie. The fourth step was the adoption of paper-money, in the form of bank-notes, which increased this economy. The fifth step was the employment of cheques; which, coupled with the last step, the estab-

lishment of the Clearing-House, has economised the use of money, alike notes and coin, to an extent not easily calculable.

Bills.—There is one more process of economising capital which deserves to be noted,—namely, the Bill-system. Bills are the currency of commerce and of wholesale trade. Their source and origin is with the mercantile community. Notes and cheques are forms of credit originating with banks; but bills are the means by which each private individual utilises his own credit. They make his capital go farther than it otherwise would. In fact they are equivalent to a temporary creation of capital. A man has a good reputation for honesty and business-talent, but his capital is not sufficient to enable him to trade to the extent which he desires, and which promises to be profitable. Then he orders £1000 in goods from a brother merchant, giving a bill in payment,—a promise to pay in money (say) three months after receipt of the goods. Before the expiry of the time, he has resold the goods, making a profit of (say) five per cent on the transaction; so that when the bill falls due, he is not only able to pay it, but has made a profit for himself of £50. Proceeding in this way—buying goods with bills at three months' date, and making five per cent on each transaction, the actual result is, that at the end of a year a merchant may make twenty per cent of profit on capital which he had only upon loan.

Mark the economy effected by this system of commercial credit. The general practice is, that a bank will discount bills for a customer to at least ten times

the amount of his average balance in the bank. Thus, if he keeps an average balance at his banker's of £1000, the bank will discount bills for him to the extent of at least £10,000. Thus he can trade to fully ten times the amount of his money in bank. By means of the bill-system, he can carry on about ten times more trade and make ten times greater profits than he otherwise could do. A commission-merchant, who does not require to sink money in his business, can by means of bills trade to ten times the amount of his whole capital. But in the case of manufacturers, and others, who have to sink money in their mills and machinery, it is only a comparatively small portion of their wealth which is deposited in bank, and which may be made a basis of bills.

The credit-system not only economises capital in the hands of those who have it, but it temporarily gives capital to those who have it not. By the credit-system, the commercial community virtually agree to lend a certain amount of their goods to any person of known integrity and business talents. It is by means of this credit-system that trade and industry in our country have attained their present marvellous development; and if it were suspended, the whole fabric of our industry would at once collapse, and the great source of our gains would be at an end.

While economising capital, the Bill-system also economises the use of money. It does so in two ways. (1.) In the Home trade. On the principle already stated—namely, that when a man has the means of getting money or goods whenever he wants them, it is

the same as if he held them—Bills to a great extent serve the purpose of money, because they are readily negotiable and convertible into money. Every merchant keeps a number of these bills in his portfolio; and before the cheque-system was fully established (and to some extent also at present), bills were passed from one merchant or manufacturer to another in payments, just as if they were money,—each merchant writing his name on the bill as it passed from hand to hand. In Birmingham, Manchester, and some other places, forty years ago, it was not uncommon to see bills which had passed through so many hands that the entire back of them was covered with the names of endorsers: and in some cases, bits of paper were pasted on and likewise covered with names. Every time one of those bills changed hands, the security for its payment was increased,—each man endorsing it, and thereafter being liable for the amount if the original acceptor of the bill should fail to meet it. In this way it was the same as if notes or coin to a like amount had been employed in payments, and the result was a corresponding economy of the currency.

(2.) In the Foreign trade, bills play a more important part as money—international currency. For example, a bill upon a Calcutta merchant held by a person in London is as good to him as a cheque upon a Calcutta bank, as an equal sum in rupees, or in notes of the Bank of Bengal. Hence to send that bill to India is the same as sending specie,—with this difference in favour of the bill, that it can be sent for the mere cost of postage, whereas the cost of transmitting specie is

considerable. Hence, when any merchant wants to transmit specie to Calcutta to make purchases or settle the trade-balances, instead of buying silver he buys those bills, and forwards them to Calcutta. Every bill thus sent abroad serves the same purpose as the export of a similar amount of specie,—thereby economising capital in the form of the precious metals; and at the same time, the payment is made more conveniently and at less expense than if specie were transmitted from one country to another.

Every bank deals in those Bills: the banks buy them (by the process called "discounting") as highly negotiable assets, suitable for the investment of banking capital. They constitute the larger portion of the securities in exchange for which the banks allow their customers to draw upon them. In fact, the "deposits" in banks are mainly constituted by an equal amount of those bills, which the banks take in security for the accommodation which they give to their customers. But the bill-system is so extensive that a special department of monetary or financial business has sprung up to meet it,—namely, the Discount-houses. The special business of these establishments is to discount those bills—*i. e.*, to buy them at their fair value,—paying the bill-holder the amount, minus the interest for the time which has to elapse before the bill falls due. When a bank discounts a bill, it does not usually pay money for it: the amount is simply placed to the credit of the person who sells to it the bill; who thereafter draws out the amount in such portions as he requires, usually by means of cheques. When a dis-

count-house buys one of those bills, it makes payment by a cheque upon the bank with which it deals. And thus nearly the whole of those immense bill-transactions are settled without the use of money, and simply by means of cheques and the Clearing-House,—the great economy of which system we have already described.

It is by means of those various processes that Capital has been so marvellously economised in this country, and that so little Money (notes or coin) is needed in carrying on our immense home and foreign trade. The monetary wants of a community, we repeat, are two-fold: (1) to carry on the daily buying and selling, and suchlike exchanges of property, among our own people and also with foreign countries; and (2) to store up in a convenient form the reserve-wealth of individuals. The amount of business in a country, whether among the community at home or with foreign countries, steadily increases, (*cæteris paribus*) requiring more money in the hands of the people to carry it on; and naturally, the reserve-wealth of individuals likewise increases, requiring more money to represent it. By means of banking, paper-money, cheques, and bills, we are now enabled to carry on our immense home and foreign trade with a wonderfully small amount of money; and at the same time to utilise the vast amount of reserve-wealth stored in the banks. If none of those economical processes were in use—if we were in the condition of our ancestors two centuries ago,—the amount of specie now required would be enormous. The fact that payments to the amount of 4600 millions a-year, equal to about 15 millions a-day, are settled

through the London Clearing-House alone, speaks volumes on this point. In truth, if every ounce of the precious ore from the new gold-mines in California and Australia had come to this country, and been kept here, this immense sum would be inadequate for our requirements, if all payments had to be made in specie and without the economy effected by banking and its appliances.

Of the various banking adjuvants of industry which we have passed in review, paper-money, in the form of bank-notes, has contributed nothing during the last quarter of a century to the marvellous industrial and commercial progress of this country. Its efficacy as a means of economising capital has remained stationary, or rather has somewhat declined. In 1834 the note-circulation of the United Kingdom was about 38 millions; in 1844 it was fully 39 millions; at present it is only 38 millions.* Moreover, 10 millions of this latter amount do not effect any economy, since they simply represent an equal amount of gold locked up in the Scotch banks and in the Bank of England in connection with the note-issues. Thus, paper-money in

* In 1844, when the present Bank Act came into operation, the note-circulation of the United Kingdom stood as follows :—

Bank of England notes (7th September),	£21,206,624
English provincial banks,	8,648,853
Irish banks,	6,354,494
Scotch banks,	3,087,209
	£39,297,180

On 5th January 1867 the note-circulation stood as follows :—

Bank of England,	£22,353,623
English provincial banks,	4,965,365
Irish banks,	6,142,983
Scotch banks,	4,630,979
	£38,092,950

this country effects a saving of only £28,000,000; and as a means of economising capital it has at best, since 1844, remained stationary.

Yet how vast in other respects has been our national progress during the same period! Within the last quarter of a century our Trade has more than trebled,—our exports and imports having increased from 130 millions sterling to fully 420 millions. The bills, or commercial currency, by which our trade is carried on, have simultaneously doubled in amount; the daily amount of bills afloat in 1843 having been about 140 millions, whereas now, according to the same authority (Mr Newmarch), the amount is about 300 millions.* During the same period, also, our banking-deposits have increased fivefold,—having risen from about 80 millions to 400 millions. And the yearly *increase* of wealth in the United Kingdom has simultaneously augmented to an uncertain but unquestionably enormous extent.

The national progress in industry and wealth exhibited by these statistics is truly wonderful. And unquestionably, so far as financial auxiliaries are concerned, the means by which this progress has been accomplished have been the extension of banking, the increased use of commercial currency (bills), and, most of all, the development of the cheque-system and the establishment of the Clearing-House.‡ In truth, Money, whether in

* It seems almost incredible that the amount of commercial bills in use has only doubled since 1843; but, in so far as reliable statistics are available, this appears to be the case.

† See *infra*, Chap. V.

‡ The following statement shows how immensely the economy effected by the clearing-system has been developed within the last thirty

the form of bank-notes or coin, hardly plays any part in the processes by which our rapidly-expanding trade is facilitated, or even in the transactions of banking. Startling as the fact may seem, not more than 5 per cent of banking-transactions are made either in notes or coin. Of the innumerable payments into banks, constituting deposits, and of the equally numerous drafts upon banks, or demands for repayment of those deposits, 95 per cent (as has already been shown) are in the form of cheques and bills; only 5 per cent being in money—*i.e.*, notes or coin.*

The grand value of a note-circulation nowadays—at least in this country, where the economy of banking is so fully developed—consists, not so much in the extent to which it economises specie, as in its power of ready expansibility, by which it can be made to neutralise the ever-recurring fluctuations in the supply of specie, or in the monetary requirements of the community. The amount of those fluctuations is comparatively trivial, and they are exceedingly transient. Nevertheless if any obstacle prevent the expansion of the note-circulation at such times, the effects are tremendous. Not only trade, but the banking-system itself, is liable to be pulled to the ground.

Money, whether bank-notes or coin, now constitutes

years:—Mr Babbage calculated that in the year 1839 the amount of banking-transactions settled through the London Clearing-House was 954 millions sterling. Reckoning on the same data, Mr Hankey estimates that in 1857 the amount so settled was 1900 millions; and that in the year ending in September 1866, it was no less than 4588 millions sterling.—*Hankey on Banking*, pp. 63, 64, and 101.

* See *supra*, pp. 6 and 27.

merely the retail currency of the country,—the medium in which we pay for the small wants of the day—for our dinner and cabs, our railway-ticket, and petty purchases in shopping. All else is done by means of cheques and bills. These cheques and bills are the great moving power,—the form in which all the larger purchases of goods and property are made: notes and coin being only needed for petty payments. Cheques and bills are to Wealth what the arm is to the body—the great agent in employing its power: notes and coin (money) are merely the fingers—the medium by which the power is applied to details. But as the power of the arm becomes almost nullified if the fingers fail, so our financial system is liable to collapse if the supply of notes becomes inadequate to the requirements of the community.

II.

ABSORPTION OF SPECIE

THERE is a feature of the present times, in connection with the economy of capital effected by Banking, which has excited much interest and discussion, and which demands special attention: namely, the recent great absorption of the precious metals, and, in a lesser degree, of Money in all forms.

Since 1849 the production of the precious metals has quadrupled in quantity: the chief increase being in gold, which is the superior metal for currency. Nevertheless the *reserve* of the precious metals available for the wants of trade and commerce is at present little, if at all, greater than it was before. The Bank of France changed its character so fundamentally in 1848 that its case cannot be referred to in this matter. But the Bank of England has remained unchanged in its constitution and circumstances since 1844; and in its case we find that, on the average of the five years ending with 1865, its stock of specie is exactly the same

as it was during the five years previous to the gold-discoveries.

We see an explanation of these facts, firstly and chiefly, in the great increase which has taken place in the foreign trade of both countries. Since 1849 the foreign trade of England has more than doubled, and the foreign trade of France has more than trebled in amount. In the case of other countries likewise, a great expansion of trade has taken place. This circumstance has occasioned a vast absorption of the precious metals. An increase of foreign trade, it is true, does not of necessity produce a greater requirement for the precious metals. If all countries were to trade mutually, and in equal amount, with one another, such international transactions might increase to any magnitude without causing a requirement for specie. The only currency required would be commercial bills. But practically this is not the case. There are countries an increase of trade with which necessitates a large employment of specie. A great portion of the increase of the foreign trade of England, France, and America has taken place with the countries of the East, especially with India and China: and as these are chiefly exporting countries—as they take from us only a small proportion of goods compared to what we import from them,—the "balance of trade" is always in their favour, and has to be liquidated on our part by a ceaseless exportation of the precious metals. In this way, most profitably and advantageously, an immense amount of the new supplies of specie has been drained away from Europe and America.*

* See also *The Economy of Capital*, pp. 50-54.

Moreover, the course of trade is always liable to transient ebb and flow: and the larger the amount of international trade which a country carries on, the larger are likely to be the occasional balances against it. Ever and anon some country *suddenly* increases its imports from some other country, and the balance thus arising must be paid in specie. The more extensive the commerce of a country, the more secure is the basis of its material industry: for, when the supply of goods from one quarter is stopped, the more easily can the loss be compensated by obtaining the required supply from other quarters. On the other hand, all such changes in the course of trade tend to produce in some quarters an adverse balance against the importing country,—liquidation of which must usually be made in specie. So that, in truth, the more extensive the commerce of a country, the greater is the liability of that country to monetary disturbance, owing to fluctuations in the ebb and flow of specie.

Thus we find (1) that a large additional amount of the precious metals has during the last sixteen years been required for, and absorbed by, the increase which has taken place in International Trade. This is a permanent absorption. And (2), owing to the increased magnitude of our foreign trade, we are very liable to temporary drains of specie in consequence of the occasional fluctuations in the course of trade. The former of these facts goes far to explain how it happens that the *reserve* of specie available for trade (viz., the stock of specie in bank) is little larger than it was previous to the discovery of the new gold-mines; the latter explains

the cause of the transient drains of specie to which we are subjected.

But there are two other facts connected with the absorption of specie which are exceedingly worthy of notice, if not for their magnitude, at least for the relation which they have with our Monetary System.

One of these is, that chiefly in consequence of the increase of the foreign trade, but partly independent of it, the domestic trade has likewise greatly increased. There is more buying and selling than there used to be twenty years ago—more wages and salaries, higher rents, &c.; and hence more currency of some kind is needed. A portion of those payments has to be made in specie. In England there are no notes of less value than £5; in France there are none below £2, 10s.: accordingly in both countries a large portion of the daily retail purchases, and all the wages of the working-classes, have to be paid in coin. Thus in England, and also in other countries, a considerable amount of specie is every year absorbed into the active metallic currency. In England the steady action of this internal drain of gold may be seen by consulting the returns of the Bank as to the additions made to the contents of the Bullion Office from abroad, and as to the total stock of gold held by the Bank: the latter, it will be found, does not increase along with the former,—and the difference shows the amount of specie which, merely passing through the Bank, becomes yearly absorbed in the active circulation of the country.

In this way, since 1843, the metallic currency of the United Kingdom has immensely increased,—not less

than 105 millions sterling of additional gold and silver coins having been issued from the Mint. The records of that establishment show that in the twenty-two years, 1844-65, gold has been coined to the amount of £114,000,000, and silver to the amount of £7,700,000, —making together £121,700,000. During the same period (as shown by the records of the Mint, supplemented by those of the Bank of England), the amount of worn gold coin withdrawn from circulation has been £14,800,000, and of worn silver coin £1,660,000: total, £16,460,000. Deducting this amount of worn and withdrawn coin from the amount of the new coins issued by the Mint, the result shows that since 1843 there has been an addition to our metallic currency of rather more than 105 millions sterling.* This gives an average of nearly five millions sterling, sunk each year in additions to the metallic currency of the country. These coins, as we have said, are needed solely for retail payments of the smallest kind,—namely, in the payment of weekly wages, and in shopping-purchases of less amount than £5. In fact, large as is the amount of capital thus sunk, it is entirely absorbed in the active circulation of the country, and goes for nothing in the larger exchanges of capital by which the national industry is mainly carried on.

Nor is this all. More money, also, whether notes or coin, is required owing to the increasing wealth of the country. As wealth increases, the deposits in bank increase; and as these deposits become larger, the banks must keep a larger amount of money in hand, in

* See Appendix, where the statistics are given in full.

order to meet this increase of their liabilities. The effects of this absorption are by no means unimportant. For example, during the last ten years the deposits in the London joint-stock banks have doubled,—they have increased from fifty millions to a hundred millions: and the amount of money kept constantly on hand in these banks alone is two or three millions greater than before. This amount, being always kept in reserve, is *de facto* immobilised: it can be used, but, speaking roundly, it never is used: it is withdrawn from the active circulation of the country. Moreover, the reserve which the London and provincial banks keep in the Bank of England has also increased: so that a smaller proportion of the Bank's "reserve" can now be relied on as fully available for the wants of that establishment than was the case twenty years ago, — a large portion of that amount belonging, in fact, not to the Bank at all, but to the other banks which have placed in its keeping a portion of their own reserves.*

Thus, then, we see (1) that an enormous absorption of the precious metals has taken place in consequence of the expansion of International trade; (2) more money, coin and notes, is needed in the hands of the people of each country, to carry on the expanding Home trade; and (3) at the same time more money is needed in bank in connection with the increasing Deposits, — which deposits represent to a large extent the total reserve-wealth of individuals.

* In 1844 the reserves of other banks kept in the Bank of England amounted to a million and a half; in November 1857 (a period of crisis), they were five and a half millions; at present their ordinary amount is probably six millions sterling at least.

All of these causes of the absorption of money will remain in force, and doubtless will continue to increase. In England especially, the chief, if not the only great source of the national growth lies in Foreign Trade. The chief source of increasing employment for the population must come from our trade with other countries. If England is to increase in population, and if the increase of wealth is to keep pace with the growth of population, her foreign trade must go on increasing in the future at least as rapidly as it has done in the past. And what is true of England at present will be true of other countries—in fact, of all countries—in course of time.

At the same time, the produce of the new gold-mines appears to have reached its maximum, or even to have begun to decline. Hence—although I doubt not other rich gold-mines will in course of time be discovered in Central Asia and in Africa—either the trade of the world will soon become fettered, or else some means must be found to allow of the present rapid expansion of trade being carried on without a corresponding increase in the supply of the precious metals.

III.

INTERNATIONAL TRADE

ADEQUATELY to exhibit the great and indeed marvellous development of International Trade which has taken place during the last twenty years would require an exposition of the commercial statistics of all the leading countries of the world. This is beyond the purpose of the present work, in which commercial statistics are made use of only in so far as they bear directly upon the monetary condition of the world, and especially of our own country. It will be more interesting, and it suffices for our purpose, to illustrate the extraordinary increase of International Trade by taking the case of two of the leading countries of the world, which also are those in which we are most interested,—namely, England and France. The commercial statistics of two such countries are especially deserving of the study of statesmen and of political economists; for these statistics throw a great light upon the social condition of the communities to which they relate, and also upon the

effects of legislation and of governmental administration upon commercial progress.

There is no feature of British power and prosperity upon which we congratulate ourselves so much as the progress of our Foreign Trade. And it is natural that we should do so, seeing that this trade with other countries furnishes the greater part of the addition which is yearly being made to the realised wealth of our country. It is this foreign trade, also, which chiefly furnishes employment for the yearly additions to our population. But in order to appreciate our commercial progress correctly, it is necessary to compare its present condition with its rate of progress in former years, and also with the expansion of trade in other countries. France is not only the nearest neighbour of England, but also the country with which a commercial comparison can most fittingly be made. While showing the great expansion which has taken place in our own commerce, let us see what has been the progress simultaneously achieved in the foreign trade of France. In doing this, we have taken pains to condense the statistics (which have been carefully compiled), so that the reader may discern their import at a glance.

Excluding the transit or emporial trade (that is to say, the portion of the imports which is not used for internal consumption, but is sent off again to other countries, and which thus appears in the returns alike as Imports and as Exports), the official returns show that the foreign trade of France in recent years has been as follows,—the amount of the exports and imports being stated in millions sterling:—

Foreign Trade of France.

	Expts.	Impts.		Expts.	Impts.		Expts.	Impts.
1851 .	46	30½	1856 .	75½	80	1861 .	77	97⅔
1852 .	50¼	40	1857 .	74⅔	75	1862 .	90	88
1853 .	61⅔	48	1858 .	75½	62½	1863 .	105¾	97
1854 .	56½	51½	1859 .	90⅔	65½	1864 .	117	101
1855 .	62⅓	63¾	1860 .	91	75	1865 .	128	111⅓
Average	55⅓	46¾	Average	81½	71½	Average	103½	99

As in 1850 the exports were 42½ and the imports 31½ millions sterling, it appears that the exports of France are now three times, and the imports three and a half times, as large as they were then: showing that the whole trade of France has more than trebled (has increased 230 per cent) during those fifteen years.

The foreign commerce of England, exclusive of the transit-trade, has during the same years been as follows:—

Foreign Trade of England.

	Expts.	Impts.		Expts.	Impts.		Expts.	Impts.
1851 .	74½	127*	1856 .	116	149	1861 .	125	183
1852 .	78	124*	1857 .	122	163¾	1862 .	124	183½
1853 .	99	140*	1858 .	116½	141½	1863 .	146½	198½
1854 .	97	133	1859 .	130½	154	1864 .	160½	222¾
1855 .	95½	122½	1860 .	136	182	1865 .	166	218
Average	89	130	Average	124	160	Average	144½	201

As in 1850 our exports were 71⅓ and our imports 115 millions sterling, it appears that since then our exports have fully, and our imports have nearly, doubled (the increase having been respectively 120 and 91 per cent): showing a total increase of the

* Previous to 1854 the Board of Trade Returns are of no use as showing the real value of our Imports. But as for several years after 1854, both the "official" and the "real value" is given, one can ascertain the ratio of difference between them, and thereby obtain the "real value" of the Imports for the three previous years.

foreign trade of England during those fifteen years of 106 per cent.

Dividing those returns into quinquennial periods, we find that the average annual amount of foreign trade carried on in each of those periods by the two countries has been as follows,—the amounts being stated as before in millions sterling :—

Quinquennial Averages.

	France.			England.		
	Exports.	Imports.	Total.	Exports.	Imports.	Total.
1851-55	55⅛	46¾	102	89	130	219
1856-60	81½	71½	153	124	160	284
1861-65	103½	99	202½	144½	201	345½

The ratio (or percentage) of *increase* of trade calculated upon the annual average of exports and imports for each of those quinquennial periods, is as follows : *—

Increase calculated on the Quinquennial Averages.

	France.			England.		
	Exports.	Imports.	Total.	Exports.	Imports.	Total.
1851-55	50 p. c.	47 p. c.	48 p. c.	46 p. c.	13 p. c.	25.8 p. c.
1856-60	47.5 ,,	50 ,,	50 ,,	40 ,,	23 ,,	29.6 ,,
1861-65	27 ,,	37.5 ,,	32 ,,	16.5 ,,	25.6 ,,	21.5 ,,

These statistics exhibit an important fact, which will be novel if not startling to the general public. They demonstrate that the foreign trade of France is increasing very much more rapidly than ours. Since 1850, it has increased 230 per cent, while the foreign trade of England has only increased 106 per cent. France under

* The annual average for the five previous years, which forms the starting-point of this computation, was as follows, in millions sterling :—

	France.			England.		
	Exports.	Imports.	Total.	Exports.	Imports.	Total.
1846-50	37	32	69	61	115	176

a system of Protection has increased in foreign trade twice as fast as England under a system of Free-trade. Moreover this ratio of increase was much greater during the ten years ending in 1860, before any change had been made in the commercial legislation of France, than it has been subsequently. The five years subsequent to the liberalising of the French tariff by the Anglo-French treaty of 1860, estimated by the annual averages, show a smaller rate of increase in the foreign commerce of France than either of the two preceding quinquennial periods. Mr Dudley Baxter is right in claiming for railways a co-ordinate power with Free-trade in developing the commerce of a country;* nevertheless, even his theory will not explain all the facts of this case. We must take into account the financial effects of the administration of Napoleon III., which, besides developing the railway-system in France, has achieved two great objects: first, the drawing forth into active use, by means of State-loans, a vast amount of wealth in the form of specie, which previously had lain inactive; and secondly, the further blow to hoarding, and the impulse to enterprise and speculation, given by the establishment of great financial companies, like the Credit Foncier, the Credit Mobilier, and others.

But if the increase of British foreign trade has been quite eclipsed by that of our neighbour France, there is

* In France, at the end of 1851, the length of the railways opened for traffic was 2124 miles; in 1865 it was 8134 miles. In England, in 1851, the length of the railways opened for traffic was about 7000 miles; at the end of 1865 it was 13,100 miles. Thus the extent of railways constructed during this period has been the same in both countries,—namely, 6000 miles, or at the rate of 430 miles a-year.

yet much in the relative commercial condition of the two countries which leaves room for self-glorification. The *amount* of our trade, on the average of the five years ending with 1865, was 70 per cent greater than that of France: yet we have only 30 millions of people, while France has 39 millions. At the same time it must be observed that, owing to the more rapid increase of French trade, the difference in *amount* is each year diminishing. For example, in 1850 the exports and imports of this country amounted to 186 millions sterling, while those of France amounted only to 74 millions,—much less than one-half those of England. But in 1865 the exports and imports of France amounted to 240 millions, or nearly two-thirds those of England, which in that year amounted to 384 millions.

As regards the transit-trade of the two countries, that of France averaged during the six years 1859-64, about 33 millions, and that of England 38 millions. But, unlike the "special trade" of the two countries, the transit-trade of England is increasing more rapidly than that of France. In round numbers, the transit-trade of the two countries has been as follows, in millions sterling:—

Transit-Trade.

	France.	England.		France.	England.
1859 . .	28	25	1862 . .	30	42
1860 . .	38	28	1863 . .	37	50
1861 . .	28	34	1864 . .	38	52

Showing that, in those six years, the transit-trade of England has doubled, while that of France has increased little more than one-third.

The transit-trade depends to a great extent upon the share of the carrying-trade of the world which a country possesses, which tends to make that country an emporium, or temporary depôt, to which merchandise is conveyed on its way to other countries. Another source of a country's transit-trade—and one in which certainly England has not declined—is the enterprise and speculation of its merchants. A merchant at Liverpool, for example, sees that a certain article (say indigo, sulphur, or saltpetre) is about to become scarce; and thereupon he hastens to forestall the market by ordering a large supply, which, when received, he ships to whichever country offers the best market—*i.e.*, the highest price for it. The third adjuvant to a transit-trade is when a country presents ample facilities for trade, in the shape of monetary and banking accommodation: so that the importing merchant may be able, if necessary, to negotiate his bills-of-lading or dock-warrants. During last summer, several vessels with cargoes of goods which had come as usual to our ports, had to weigh anchor again and sail to France: the merchants finding it impossible to obtain their usual banking accommodation in England even at 10 per cent., whereas they could get it readily in France at 4 per cent. Nevertheless, despite the greater frequency of monetary crises in this country, a superiority in the other auxiliaries of a transit-trade secures for England a more rapid increase than falls to the share of France.

Having thus shown the amount and increase of the foreign trade carried on respectively by France and England, alike absolutely, and also relatively to the

population of the two countries, we shall complete our investigation by pointing out some other features, not less important, presented by the commercial statistics of the two countries.

Foremost among these is the very different relation in the trade of the two countries, which the amount of the imports bears to that of the exports. As appears from the statistics already given, the case, during the fifteen years ending in 1865, has stood thus, — the average annual amount for each quinquennial period being stated in millions sterling:—

	France. Excess of Exports.	England. Excess of Imports.
1851-55 .	8½ mils. or 15 per ct.	40½ millions or 46 per cent.
1856-60 .	9½ ,, or 11.7 ,,	34 ,, or 27.4 ,,
1861-65 .	4½ ,, or 4.3 ,,	56½ ,, or 39 ,,

On the whole fifteen years, the trade of France shows an excess of exports over imports to the amount of 115 millions sterling; while the trade of Great Britain during the same period shows an aggregate excess of imports over exports to the amount of 655 millions. Also, in the first of those three quinquennial periods, the excess of the exports was 15 per cent over the amount of imports, in the case of France; while in the last of those periods it was only 4 per cent. In the case of England, the excess of imports in the first period was 46 per cent over the amount of exports; and in the last period it was considerably less—namely, 39 per cent: a figure which also represents the average annual excess of our imports during the fifteen years. It also appears that in France the imports are steadily increas-

ing in proportion to the exports; so that, if this state of matters continues, in a few years hence, France will import more largely than she will export.

The contrast which the commercial statistics of France and England exhibit in regard to the balance of trade of the two countries calls for special notice. In order to investigate it, let us take 1863 as an average year, and analyse the imports and exports of the two countries. A single glance suffices to show that a large portion of the excess of the imports into the United Kingdom over our exports is in the form of Food—of articles consumed by our population either as necessaries or luxuries; whereas the trade of France exhibits no corresponding feature. In 1863 the trade of France in articles of Food (using the word in its widest sense) was as follows :—

Food-Trade of France.

Imports.		Exports.	
Corn, Flour, &c.	£2,320,000	Grain and Flour,	£4,584,000
Live Stock,	3,050,000	Live Stock,	1,353,000
Bacon, Butter, Cheese,	1,328,000	Bacon, Butter, Cheese, Eggs,	4,388,000
Rice,	491,000		
Fish,	1,236,000	Fish,	909,000
Fruit,	670,000	Fruit,	766,000
Sugar and Molasses,	6,000,000	Sugar,	4,471,000
Coffee and Cocoa,	3,520,000	Wines,	11,224,000
Tea,	60,000	Spirits, &c.,	2,356,000
Wine,	226,000		£30,051,000
Spirits,	247,000		19,983,000
Beer,	67,000		
Tobacco,	768,000	Excess of Food-Exp. over Imp.	£10,068,000
	£19,983,000		

In the same year, 1863, the trade of England in articles of Food showed no appreciable amount of exports, while the imports were as follows :—

Imports of Food—England.

Corn and Flour,	£26,000,000	Tea, . . .	£10,666,000
Bacon, Butter, and Cheese, . .	8,800,000	Coffee, . . .	4,155,000
Live Stock, . .	2,600,000	Wine, . . .	4,500,000
Rice, . . .	1,866,000	Spirits, . . .	1,700,000
Fruit, . . .	1,562,000	Tobacco, . .	3,000,000
Sugar, . . .	12,368,000	Total, .	£77,217,000

From these statistics it appears that while France exports about 10 millions more of food-articles than she imports, England imports 77 millions, and exports none. The cause of this striking difference is twofold. In the first place, the area of cultivable land in England compared with her population is very much less than in the case of France. In the second place, our manufacturing industry—our power of importing raw material and exporting it in a manufactured form with a profit to ourselves—is very much greater than in the case of France. It is this manufacturing-trade for export which in recent times has been the main source of the *growth* of this country, alike in wealth and in population. But for it, we should not be able to maintain so large a population as we do,—certainly we could not maintain it in anything like its present condition of wellbeing. Doubtless there are large tracts of unreclaimed land in the British Isles which are susceptible of cultivation; and as the economy of agricultural labour increases, by means of the steam-plough and improved machinery, a portion of this area will be brought under cultivation. But, as our population is steadily increasing—and long may it do so!—the addition to our supplies of food from this source will hardly keep pace with the increased

demand: so that the proportion of our food-supplies which we import will certainly continue to increase. In truth, the best soils being already occupied, we find it more profitable to import cereal food from other countries than to raise a large additional supply of it at home by reclaiming the inferior soils. And the profit upon our manufacturing industry is so great that we actually can import food for the population so employed, and yet, by exporting the produce of their labour, place the world at large more in our debt than we are to the countries from which we import our food-supplies.

It is natural to expect that this great diversity in the foreign trade of France and England should be accompanied by a corresponding difference in the current of the precious metals to and from those countries. To some extent this expectation is justified by the facts: but, as will immediately appear, the correspondence is very small,—proving that there is some other, and most powerful, influence at work, to which the statistics of Trade alone furnish no clue. First, as regards France. The following are the exports and imports of merchandise, and also of specie, for the last nine years,—a period which unfortunately we cannot go beyond, for purposes of comparison, owing to the circumstance that it is only since 1857 that the exports of specie from England have been registered at the Custom-House:—

Trade of France.

	Merchandise.		Gold and Silver.	
	Imports.	Exports.	Imports.	Exports.
1858 .	62½	75½	28⅔	9⅓
1859 .	65½	90⅔	37½	22¾
1860 .	75	91	21	18
1861 .	97⅔	77	16½	20
1862 .	88	90	21⅓	18
1863 .	87	105¾	21⅓	23½
1864 .	101	117	29⅓	26
1865 .	101⅓	128	28¼	17⅓
	678	774½	204	155
	Excess of Exp., £96,500,000.		Excess of Imp., £49,000,000	

Here, then, we see that the balance of trade—*i.e.*, of the imports and exports of merchandise—has during these eight years been in favour of France to the amount of 96½ millions sterling; while the imports of specie have exceeded the exports only to the amount of 49 millions. What has become of the remaining 47 millions?

Finally, as to England, the exports and imports of merchandise, and also of specie, during the same period have been as follows,—the amounts being, as heretofore, given in millions sterling:—

Trade of England.

	Merchandise.		Gold and Silver.	
	Imports.	Exports.	Imports.	Exports.
1858 .	141½	116½	29½	19½
1859 .	154	130½	36¾	35⅓
1860 .	182	136	23	25½
1861 .	183	125	18¾	21
1862 .	183½	124	31½	29½
1863 .	198½	146½	30	26½
1864 .	222¾	160½	27⅔	23
1865 .	218	166	21½	15
	1483¼	1105	218½	195½
	Excess of Imp., £378,250,000		Excess of Imp., £23,000,000	

In the case of France, where the exports of merchandise exceed the imports, specie to half the amount of this excess flows into the country in trade-payments, leaving the other half to be settled by other means. In the case of England, although the imports of merchandise vastly exceed the exports, no specie goes abroad to pay for any portion of this excess of imports,—on the contrary, more specie comes to us than goes away. This fact is far more startling than the analogous result in the case of France. Although, as regards the export and import of Merchandise, there has been an enormous balance against this country, nevertheless our stock of Specie simultaneously increases. How this happens—in what way this result, seemingly so incongruous, is to be explained,—we shall show in a separate chapter.

IV.

THE BALANCE OF TRADE

THERE is a peculiar feature in the commercial condition of the United Kingdom which distinguishes it from that of any other country in the world. Our imports of merchandise largely exceed our exports. This is an exceptional condition of affairs, although doubtless some other countries ere long will present the same phenomenon. At present, the normal condition of countries is to export more largely than they import. India, for example, exports a far larger amount of merchandise than it imports; it sends forth for sale in other countries a much larger quantity of produce or manufactures than it buys from those countries. China is in a similar position. In a lesser degree the countries of Europe present the same feature. Even our neighbour, France, whose commercial condition most nearly approximates to our own, still continues to export more largely than it imports. The British Isles, on the other hand, import from other countries a vastly

larger amount of merchandise than they export. The following are the statistics of the matter for the last sixteen years, founded upon the official returns of the Board of Trade:—

Excess of Imports over Exports.

1851*. . 52 millions	1856 . . 33 millions	1861 . . 58 millions
1852*. . 46 „	1857 . . 42 „	1862 . . 59 „
1853*. . 41 „	1858 . . 25 „	1863 . . 52 „
1854 . . 36 „	1859 . . 23 „	1864 . . 62 „
1855 . . 27 „	1860 . . 46 „	1865 . . 52 „
Average excess, 40 millions.	Average excess, 34 millions.	Average excess, 56½ millions.

Since the beginning of 1851 we have bought and imported from other countries fully 650 millions sterling more merchandise than we have exported and sold to them! This appears a most formidable statement of national indebtedness. Again and again during the last forty years public attention has been called to such statistics as a proof that the country was running headlong into debt and ruin. But somehow or other, inexplicable to those prophets of evil, and never fully explained by any one, the country continues to prosper, and to prosper marvellously. How is this to be accounted for?

In the first place, we must point out that the excess in value of our imports over our exports, as shown in the official statistics, is in great part illusory. The "declared value" of the exports and the "real value" of the imports (as given in the Board of Trade Returns) are not synonymous terms which can be made the basis of an equation. The "real value" of the

* See footnote, p. 48.

imports represents the selling-price of the goods; but the "declared value" of the exports does not. In order to get the "real value" or selling-price of the exported goods, we must add the costs of freightage, of commission, insurance, and other charges, as well as the profits of the exporting merchant. For example, a wholesale English merchant gives an order to a commission-merchant in London or Liverpool to procure for him certain goods from India and America. The commission-merchant transmits the order to his agents in Calcutta and New York, who buy the goods and ship them for England. The value of these goods as shipped at Calcutta and New York would be equivalent to the "declared value" of our exports, but it would fall much short of the "real value" of these goods when they come to figure as imports into this country. The "declared value" is the value of goods when shipped from the country from which they are exported; but the "real value" is the actual price at which these foreign goods are sold in our markets.

Say that a Calcutta merchant consigns to a commission-house in London 400 qrs. of linseed, the cost of which at Calcutta is 55s. per quarter free on board. Or that a New York merchant consigns in like manner 400 qrs. of wheat, of which the current price is 64s. 6d. free on board. Then, before we can arrive at the "real value" or selling-price of these articles in England, the following charges have to be added:—

CALCUTTA TRADE.

400 qrs. linseed, f.o.b. at Calcutta, at 55s. per qr., .				£1100	0	0
Charges:—						
Freight, at 45s. per ton, say on 70 tons, .	£157	10	0			
Insurance, 35s. per cent, . . .	19	5	0			
Lighterage, Landing, Metage, &c., 2 per cent,	22	0	0			
				198	15	0
				£1298	15	0
Brokerage on £1298 15s., 1 per cent, .	£12	19	9			
Commission on ditto, 5 per cent, . .	64	18	7			
				77	18	4
				£1376	13	4
Profit of Importing Merchant, (say) 10 per cent on £1100, ...				£110	0	0
"Real value," or selling-price in England, . .				£1486	13	4

NEW YORK TRADE.

400 qrs. wheat, f.o.b. at New York, at 64s. 6d. per qr.,				£1290	0	0
Charges:—						
Freight, at 4s. 6d. per qr., . . .	£90	0	0			
Insurance, 35s. per cent, ...	22	11	6			
Lighterage, Landing, Metage, &c., 2 per cent,	25	16	0			
Duty, 1s. per qr., ...	20	0	0			
				£158	7	6
				£1448	7	6
Factorage, 1s. per quarter, ...				20	0	0
Commission on £1468, 7s. 6d., 2½ per cent, . .				36	14	0
				£1505	1	6
Profit of Importing Merchant, (say) 7½ per cent on £1290, ...				96	15	0
"Real value," or selling-price in England, . .				£1601	16	6

In the first of these cases, the difference between the "declared value," or price of the goods when shipped, and their "real value," or selling-price in the country

into which they are imported, is £386,—equal to an addition of 35 per cent on the declared value. In the second case, the difference is £311, or 24¼ per cent. If we strike an average of those different rates of charges —viz., those usual in the trade with Calcutta and with New York—we shall have a fair average of the addition which must be made to the "declared value" of our exports, in order to get the real value, or actual selling-price of these goods in the foreign markets to which they are sent. In other words, before we can strike a true balance between our exports and imports of merchandise, we must add 30 per cent to the "declared value" of the exports.

This is the true statement of the Balance of Trade: it is the correct interpretation of the statistics of the Board of Trade. Hence it appears that a considerable portion of the trade-balance, as given in those official returns, is illusory—is nominal only, not real.

Adding 30 per cent to the declared value of our exports, in order to get their real value, the correct statement of the balance of trade during the last six years is as follows, in millions sterling:—

			Excess.		
	Exports.	Imports.	Exports.	Imports.	
1861	162	183	...	21	
1862	161	183½	...	22½	
1863	190	198½	...	8½	68¾
1864	208	222¾	...	14¾	
1865	216	218	...	2	
1866	245	238¾	6¼	...	

In this way the balance of Trade against this country is reduced to comparatively small proportions. In fact the Trade-balance against us in 1865 appears to have

been merely nominal, only 2 millions; and last year it appears to have been fully 6 millions in our favour. But this does not exhaust the question. There is a Financial balance also which has to be taken into account,—in other words, the difference between the amount of wealth which we in any year invest in foreign countries and the amount which we simultaneously receive from abroad as interest upon such investments previously made.

The investments of British wealth in foreign countries during any year have the same effect upon the financial balance between this country and the rest of the world as if an equal addition were made to our imports of merchandise. Although by such investments we are really placing other countries in debt to us, the first effect of those transactions upon "the exchanges" is the same as if we had become in debt to other countries. If, during any year, 20 millions of British capital are invested abroad, these 20 millions have to be supplied to other countries by our capitalists who make the investments. Some portion of this amount doubtless is expended in this country: for example, in the furnishing of rails and engines for the foreign railways, or ships and munitions of war for the foreign Governments to whom the loans are made, or in payment of interest on the previously contracted debt of those Governments to English bond-holders, and suchlike payments. But the remainder and chief portion is actually expended abroad, and tends to form a financial balance against this country. But while the investments of British wealth abroad in any year

proportionately swell the balance against us for that year, it is equally true that the returns upon British wealth *previously* invested abroad must be put on the other side of the account. While the former payments, which have to be sent abroad, must be placed to the debtor side of the national ledger; the latter, which have to be sent hither, must be placed to the national credit,—and they are available to liquidate the yearly liabilities, alike financial and commercial, which we incur to other countries.

The facts of the case, then, are as follows:—Firstly (after striking the real balance between our Exports and Imports of merchandise), there is usually an annual Commercial balance against this country: and this adverse balance, on the average of the last six years, amounted to 10 millions sterling. Secondly, there is the annual amount of investments of British wealth abroad: which amount constitutes, for each particular year (for the year during which those investments are made), a *primâ facie* adverse Financial balance, in addition to the usually adverse Commercial balance. At present there are no means of determining the actual amount of this Financial balance; but we can show conclusively that both it and the usual Commercial balance against this country are more than settled. The settlement of an adverse balance can be effected only in two ways: namely, either by an export of specie, or else by the yearly payments of interest due upon British wealth *previously* invested abroad. If the balance is not settled by one of those means, we may safely infer that it is settled by the other.

An export of specie is not necessarily a proof of national indebtedness, — it may arise simply from a temporary monetary disturbance, or from a change in the currents of trade; but it is a necessary and inevitable result when a country actually becomes in debt to its neighbours—when the International Balance (*i. e.*, the balance alike of the commercial and of the financial transactions of a country) is really against it. If a country is really in debt, it must ultimately pay the balance of its indebtedness by exports of specie; and this liquidation cannot be long delayed. On the other hand, if we find specie steadily flowing into a country over a series of years, this is a substantial proof that that country is not in a state of indebtedness to the rest of the world. Now, in the case of England, the movements of the precious metals show plainly that as a nation we are not in debt. On the contrary, much more specie has been flowing into the United Kingdom than has flowed out of it. For example, during the last six years, the imports of Gold have each year exceeded the exports by the following amounts:—

Gold—Excess of Imports over Exports.

1861, . .	£925,600	1864, . .	£3,618,000
1862, . .	3,892,000	1865, . .	6,820,000
1863, . .	3,832,000	1866, . .	10,767,000

If we take gold and silver together, the result is nearly the same. The Board of Trade returns show an excess of imports of the precious metals over the exports in every year save the first of the series:—

Gold and Silver—Balance of Imports and Exports.

1861, . .	£2,065,000	1864, . .	£4,476,000
1862, . .	2,330,000	1865, . .	9,281,000
1863, . .	3,427,000	1866, . .	12,616,000

Hence it appears that so far from there being a steady drain of specie from this country (as there would be if the International Balance were against us), no less than 30 millions have been added to our stock of the precious metals since 1860, although simultaneously (as shown on p. 63) there has been a *real* Commercial balance against us of 63 millions sterling. Nay more, the yearly addition to our specie has of late years been largely increasing,—having risen from $2\frac{1}{3}$ millions in 1862 to upwards of $12\frac{1}{2}$ millions last year. These figures totally upset the idea that there is any International Balance against this country. They demonstrate exactly the reverse. Moreover, they show that, during the last four years, the International Balance has become more and more in our favour,—having risen to fully 9 millions in 1865, and to fully $12\frac{1}{2}$ millions in 1866.

The real cause of the ever-increasing excess of our imports over our exports is the increase of our national wealth, which permits an augmented expenditure in the comforts and luxuries of life; while, at the same time, the adverse commercial balance thus occasioned is more than met by the revenue ever coming into this country from investments of British wealth abroad,—from the profit upon that portion of the yearly additions to our wealth which regularly overflows, seeking and finding a profitable investment in other countries. This sum

—this Financial balance or annual return upon British wealth invested abroad—it is which, being annually due to this country, more than redresses the Commercial balance, which is almost always against us.

It would be most desirable to know what the amount of this Financial balance is, which thus redresses the usually adverse Commercial balance of this country. Unfortunately, as there are at present no statistics available for computing the total amount of British wealth invested in foreign countries, the profit or yearly return upon those investments must be a matter of conjecture. Nevertheless the facts above stated suggest the following inference: Since during the last six years there has been on the average an adverse Commercial balance of fully 10 millions a-year, while at the same time the balance of specie movements has been in our favour to an amount averaging 5 millions a-year, it seems that there must be an annual Financial balance in our favour to the extent of fully 15 millions,—that is to say, the interest due to our capitalists from abroad must exceed by 15 millions the annual amount of the *new* investments of British capital in foreign countries. This much, in truth, may be stated as a fact, rather than as a conjecture. But what is the annual amount of the *new* investments of British wealth abroad?—which amount must be added to these 15 millions before we can arrive at the total yearly profit on our foreign investments. Here we are at a loss. But the case of France may help us in making an estimate for our own country.

M. Emile Pereire, a reliable authority, stated in his evidence before the French Government Inquiry into

Banking, that the amount of French capital invested in other countries (in foreign loans, railways, &c.) between the years 1852 and 1864 was 364 millions sterling: of which amount 170 millions were invested in loans, and 190 millions in joint-stock companies. This gives an average for those 12 years of 30 millions annually invested abroad; and since 30 millions was the average for the whole period, the actual amount for the last year of the period (1864) would naturally be somewhat greater. The French capital invested during the same period in joint-stock companies at home amounted only to 200 millions sterling,—little more than one-half of the amount contemporaneously invested abroad. Since France has invested 360 millions sterling in foreign loans and enterprises in twelve years, is it an excessive estimate that the total amount of British wealth invested in foreign countries is at present nearly thrice as large, say 1000 millions sterling? This, at 5 per cent, would yield 50 millions a-year: a sum which, after deducting 35 millions as probably neutralised by an equal amount of *new* investments, would leave the 15 millions of Financial balance which, as has been shown, not only neutralises the adverse Commercial balance, but serves to bring into the country specie to the amount of 5 millions a-year. According to this estimate, the annual amount of new investments of British wealth abroad is reckoned as little greater than the average foreign investments of France during the twelve years ending in 1864, which was 30 millions.

V.

WHAT IS CAPITAL?

THE term "Capital"—either alone, or variously qualified as "fixed," "floating," and "loanable"—has come greatly into use in discussions upon monetary and financial questions, without any clear definition having as yet been attached to it. The public has become familiar with the term from its frequent occurrence in pamphlets and in newspapers; but it is the word only which has thus become familiar,—for its actual or legitimate meaning we have still to seek. There has not even been a discussion as to what the word really signifies. Each man uses the word in his own way, careless of the meaning attached to it by others. The general public, in truth, care so little to inquire into the facts and principles of monetary science, or indeed of any science, that they are only too thankful to be furnished with a verbal formula which purports to explain matters which are beyond their full comprehension. Just as a metaphysician thinks he has done a great feat when he

transmutes a common phrase into one of much greater length and less general intelligibility; or as a man of science thinks he explains a "network" by describing it as a "series of reticulations;" so does many a writer consider that he throws a flood of light upon some monetary or commercial crisis by affirming that it has been occasioned by "a want of capital," by a "too great conversion of floating into fixed capital," or suchlike phrases, — without condescending to inform the public, or to clear up his own ideas, by explaining what he means by those phrases. Such terms would be exceedingly useful as shorthand expressions, like the signs of algebra, if their meaning were definitely fixed: but at present they are, for the solid purposes of reasoning, little better than the x in algebra—a definite sign representing an unknown quantity.

What, then, is "fixed," and what is "floating" capital? Unfortunately we cannot come to the point so quickly as this. The word "capital" itself is a term for which no definite meaning has yet been established. In fact the chaotic condition of a portion of the terminology alike of monetary and of politico-economic science is one of the greatest obstacles to sound discussion. Hardly any writer has thought it worth his while to give a deliberate definition of the word "capital;" and among the many writers who use the word, we have not met with any two who quite agree in the meaning which, obviously, if not explicitly, they attach to it. Indeed, nothing is more common than to find a writer using the word in several different senses, confusedly,—that

is to say, without explanation, and apparently without being conscious that he does so.

As used in financial science, Capital is a new word: it is a technical phrase differing in signification from the original and general use of the word. The dictionary tells us nothing about it. Old Dr Johnson apparently had never heard of it,—at least he takes no note of it. And if we turn to his successors in lexicography, we are left equally at fault. We find "capital" explained as the chief city of a country or of a district,—we find it used as an adjective signifying "chief," "most important," or "excellent:" but not a word as to its meaning as now employed in monetary and financial disquisitions. The word is explained in accordance with its etymology, — as relating to the "head," or most important part of any body, whether individual or corporate, and thence as applicable to the main point in all matters. Hence, when a financial meaning is given to the word, it is described solely as the capital sum, or main-body of wealth, in contradistinction to the interest (whether in the form of rent, dividends, or other annual payments) accruing to the owner of the wealth. This of course, although a legitimate and correct meaning of the term, is not that in which "capital" is used in monetary and politico-economic discussions. Nevertheless the principle of the definition is correct; and if we extend it to the wider sense in which the word is used in financial or economical science, the natural meaning of "capital" would correspond very nearly with the Greek phrase το χρημα, or the Latin *res*,—i. e., "*the* thing,"—to wit, property in the

form most efficient for supplying the wants and desires of its owner.

Leaving the dictionaries and etymology, let us see what light is thrown on the matter by the writings of more or less established authorities in political economy and monetary science. We turned first to a work of the late Mr James Wilson, entitled "Capital, Currency, and Banking." Unfortunately this book, though distinguished by admirable clearness and ability, is only a republication of many short and more or less fragmentary articles. After turning over its closely printed and typographically repellant pages, the only definition which we could find is (p. 103), that "all capital consists of accumulated labour, represented by commodities." This is a broad definition, but it is somewhat vague in its latter clause, seeing that it leaves the word "commodities" undefined. Next, as we glanced over our book-shelves, we saw a "Catechism of the Currency," by the late Mr John Taylor, a gentleman whose writings are those of a man who gave himself earnestly and carefully to whatever work he took in hand. But in his "Catechism," or book of monetary and financial definitions, published in 1836, no mention is made of "capital" at all. Finally we took down Mr Mill's standard work on Political Economy, and turned to a chapter on the very theme we were investigating. But the hopes raised by the title of the chapter were far from being realised. We were floored at once by finding that the author considers that no one can say whether anything is capital or not except the man who possesses it. To quote his own words,—

"The distinction between Capital and Not-capital does not lie in the kind of commodities, but in the mind of the capitalist,—in his will to employ them for one purpose rather than another." (Manifestly there is a slip here: Mr Mill ought to have said, "in the mind of the owner of the commodities;" for if the commodities are "Not-capital," their owner cannot be a capitalist.) And he adds: "All property, however ill adapted in itself for the use of labourers, is a part of capital, so soon as it, or the value to be received from it, is set apart for productive investment." Mr Mill's definition of capital, therefore, is somewhat metaphysical. Whether a commodity —corn, cattle, or coin, &c.—be capital or not, he says, depends entirely on the mind or intention of its owner. This does not help us much. Neither does his secondary explanation,—namely, that *anything* becomes capital as soon as its owner intends to employ it in productive investment, howsoever ill adapted for the purpose such property may be.

Some of Mr Mill's explanations of Capital are much more puzzling than these. For example, he says that the idea that Money and Capital are in any way synonymous is a supposition only cherished by "persons wholly unused to reflect on the subject." He adds:—"Money is no more synonymous with capital than it is with wealth. Money cannot in itself perform any part of the office of Capital, since it can afford no assistance to production." These are startling assertions. That money can afford no assistance to production is, we cannot help saying, an absurdity. The special use of Money is to facilitate production: in

truth, the origin and continued use of money have been due to the very fact that money so greatly facilitates production that it is advantageous to withdraw an amount of human labour from direct production in order to provide currency in the form of the precious metals.* And if we do not equally contest Mr Mill's statements that money is not wealth and not capital, and that it cannot perform any part of the office of capital, it is only because we cannot fully understand his definition of that word. Mr Mill's point of view is occasionally so exceptional that one is at a loss to recognise the things which he describes: so that even the most practical matters (such as the above) become transmogrified, and are presented in a shape dissimilar from that which they wear in ordinary life.

If we turn to the large and elaborate work of Mr M'Leod upon the "Theory and Practice of Banking," we find quite a different definition of capital,—a definition, also, alike more intelligible and of more practical application. Instead of holding that Money is not capital, Mr M'Leod regards it as the chief form of Capital,—while including, of course, many other things under that category. He defines Capital to be "anything which a man can trade with; or which helps him to economise labour; any property or quality [even "a good character"] which he possesses, which enables him to increase his wealth; any instrument however humble, or any contrivance however simple, which abridges labour and increases production." †

* See *infra*, Chapter VII.

† *Theory and Practice of Banking* (edit. 1855), p. 62.

Money is not Capital, says Mill: or at least—and we believe this is the truer statement of his views—Money is not necessarily Capital. Money is Capital, says M'Leod. Why this difference of opinion? It seems to us that this difference, like many others in monetary science, arises simply from the different point of view taken by the various thinkers. Were they to judge the matter from the same point of view, the difference would almost wholly disappear: and so far as any divergence of opinion might remain, owing to the substantial difference as to the facts of the case which seems to us to exist between these two authors, Mr M'Leod would be nearer the truth than Mr Mill. The latter seems to believe that all money is in constant use for carrying on trade; and that, being already in use for this purpose, it is not available for carrying on more trade. Therefore, says Mr Mill, Money is not Capital: being already employed in reproduction, its power for reproduction (or as Capital) is exhausted. This would be true, if the facts were in perfect accordance with the statement. But Mr Mill overlooks the fact that Money is used in the storing of Wealth (*i.e.*, as reserve-wealth, or capital) as well as in actual use as currency, in facilitating exchanges of property. Apart from the fact that in many countries where the banking-system is not fully developed, a very considerable portion of Money is hoarded (which is the case even in France), let us take the case of our own country, where (speaking roundly) no such hoarding is practised.

What becomes of the money which (to use the common phrase) is in "active circulation" in this country? In

what condition does it exist? All writers speak of the coins and notes so employed as if they were *in vacuo*—in a limbo where they belong to no one in particular,—as if, like Mahomet's coffin, which is believed to remain suspended between heaven and earth, they existed in a middle state between the payer and receiver, and belonging to neither. This, of course, like many other prevalent notions in monetary science, is a mistake: it is sheer nonsense. The money said to be in "active circulation" means simply the amount of money which is not in bank. But it is all in the possession of individuals, who can employ it each in his own way. Every man keeps on hand so many coins or notes for his current wants. He keeps at home so much money for small household wants, and carries so much also in his purse for cabs, dinners, or casual purchases or payments. Even the working-man leaves so many shillings at home, and carries a smaller trifle in his pocket for his own daily wants. It is in this fashion that Money is, to use the common phrase, "absorbed in the circulation,"—and in no other way. Hence, in regard to the many millions of coin and notes "absorbed in circulation," it is a mistake to suppose that they cannot figure as capital. They are the reserve-wealth of individuals for the day or the week, or the fortnight. Moreover, they are employed in reproduction,—if that be "reproductive" expenditure which enables a man to do more work, or to carry on as much work as before. So that this Money is certainly Individual Capital, even if it be not National Capital also. It is true this Money is not in bank—it is not in the great loan-market, to which

men usually go for monetary accommodation. But that is all. *It* also in a small way may be loaned, or employed in extending productive industry. And hence, all Money, whether "absorbed in circulation" or deposited in bank, is reserve-wealth belonging to individuals. Nevertheless, it is true that all wealth is less potent, is less economised for productive investment, when it is diffused among millions than when it is concentrated in the keeping of banks.

In all discussions on this subject, one important point must be noted at the outset: namely, the distinction between national capital and the capital of an individual. What is indubitably capital as regards an individual may not be an addition to the national capital,—as we shall show in the sequel. Mr Mill, in his chapter on Capital, does not clearly draw this distinction, but he certainly sees it: Mr Wilson and Mr M'Leod, on the other hand, do not take notice of it. Mr Mill evidently means his definitions of capital to apply chiefly to national capital: but he also speaks of the capital of individuals. What he says in regard to the capital of individuals (as distinct from national capital) may be summed up in two statements. (1) That a right to an annuity or yearly payment, whether obtained by the possession of Government securities or otherwise, is capital. (2) That if A lends £1000 to B, the sum in the hands of B "is as much capital as if it belonged to B;" while, at the same time, "A is as rich as before,—he has no longer his thousand pounds, but he has a lien on the land or other property of B, which he can sell for that amount." These statements

we hold to be correct: and we regret that it was apart from Mr Mill's general purpose to treat more fully this phase of the subject,—namely, of capital as belonging to individuals.

It is obvious that Money in the form of specie is Capital according to the definitions of Wilson and M'Leod: for the precious metals are an embodiment of "accumulated labour in the form of commodities," which is Wilson's definition of Capital. Notes also, as well as coin, are "a thing which a man may trade with," which is one of the definitions given by M'Leod, and at the same time they are comprised under all the other definitions of Capital given by that author. Mr Mill, as we have shown above, speaks dubiously, and not very intelligibly, upon both of these points; but as he includes a bond over property as Capital *quoad* individuals—as representing Value convertible into Money—it follows, *a fortiori*, that specie and bank-notes are, or may be, according to his views, Capital of the same kind,—*i. e.*, capital *quoad* individuals.

Bank-notes, commercial bills, and bonds over property, may not constitute National Capital, but unquestionably they are forms of Individual Capital: they are real wealth as regards the holders of them. As regards bank-notes there can be little dispute. That the thousand pounds in bank-notes which a man may have in his pocket are capital, quite as much as if they were a thousand sovereigns, need not, we think, be discussed. Notes which are convertible into coin are identical in value with coin. But what of commercial bills, and bonds over property of any kind? When a mer-

chant sells to another merchant goods to the value of £1000, and gets a bill for the amount payable one month after date, is this bill "Capital," or is it not? Clearly, if the merchant had not made this sale he would have possessed the goods, — and these goods unquestionably are capital. Having sold the goods, he becomes possessed of a perfect equivalent (otherwise he would not make the exchange)—namely, the price of the goods in a form convertible into money of the realm at the expiry of thirty days. It is the same as if he became possessed of a railway-debenture, or of an Exchequer bill, payable in one month's time. Nay, more, this bill is as much "capital" as a bank's deposit-receipt is to a person who has deposited £1000 in a bank at interest, subject to a month's notice before withdrawal. No one disputes that an Exchequer bill, or a railway-debenture, or a bank's deposit-receipt, is Capital *quoad* its possessor. A commercial bill is a document of the same kind: it is a bond convertible into Money at a certain date.

Bills and bonds of all kinds are clearly, though not expressly, included in Mr M'Leod's definition of Capital, quoted above; and Mr Mill expressly, and repeatedly, recognises bonds as real capital *quoad* their possessors. In truth the whole cause of the confusion to be found in many treatises on this subject, arises from the fact that the writers have not observed the substantial difference (which we have already alluded to) between Individual and National capital. The bills which some individuals hold upon others of the same community do not, of course, constitute an addition

to the realised wealth of that country: they are of no use whatever in settling an international balance: but they are thoroughly efficient in settling accounts between members of the same community. A man who lends his money or goods to another does not thereby lose the value of them. He will not part with them without a perfectly adequate equivalent,—something that is equal in value to that which he has parted with. Hence the bill or bond which he gets in exchange possesses equal value to the property which he gives away. And since it is equal in Value, there is, for all practical purposes, no more to be said. If the bill be equal in value (*i. e.*, exchangeable for the same amount of money) to the property parted with—and it obviously must be so, as no man will take less,—the bill is manifestly as truly capital as regards its possessor as the goods which he gave away.

Such, then, are the existing, and more or less conflicting, definitions of Capital by writers of acknowledged reputation,—by able men who have specially studied the subject: as to the manner in which the term is used by ordinary writers we need not speak, for it is a mere chaos. By Mr Wilson, the most practical and in many respects the ablest authority on the subject, Capital is used to signify accumulated labour, or realised wealth, in the shape of commodities of all kinds—whether reserve-wealth or not, and irrespective of the use to which it is put. Mr M'Leod gives the word a still wider meaning; defining it as "anything which enables a man to increase his wealth,"—even though it only be a good character; "or any contriv-

ance which economises labour," and thereby *pro tanto* "increases production." Lastly, Mr Mill holds that property of any kind is capital if it is, or is meant to be, applied to productive industry—whatever that may be.

We need not argue this point further. It involves simply a question of terminology, of no real importance in practical discussions, seeing that the whole subject might, in fact, be discussed without using the word Capital at all.* At the same time—since the use of this vague word cannot now be ignored—we hold with Mr Mill, and upon our own grounds above specified, that bills and bonds *are* Capital as regards their holders. And it is only by confounding Individual with National capital, or by not seeing any difference between them, that some writers in their own confused way hold an opposite opinion. Let us add, also, that in all works upon Monetary Science, it is Individual Capital only, or almost only, that ever comes under discussion. It is not the Nation that applies to a bank for accommodation, but an individual: and it is securities held by individuals only that a bank has to deal with.

As regards his use of the word "Capital," in its relation to National wealth,—taking the solid substance of his explanation apart from the perplexing statements in which he envelops it,—it seems to us that Mr Mill has narrowed the meaning of the term, without

* The frequency with which the word Capital is used in monetary discussions is a circumstance to be regretted, as it has imported into the science a new and vague word, which was not needed, and the interpretation of which has become apparently as important a matter as the elucidation of the actual facts and principles of the science.

attaining any compensating clearness or precision. He restricts the word "capital," as regards a nation, to the amount of property which is meant by its possessors to be employed in productive industry; but this amount includes a portion which is not actually so employed, though meant to be so,—and also another portion of the country's reserve-wealth which might be so employed, but for the apathy of its possessors (which apathy generally is occasioned simply by a want of trading facilities). Thus Mr Mill's definition of capital is somewhat narrower even than that which belongs to "loanable capital" (see *infra*, Chap. X.), which is but one of the subdivisions of the category.

Mr Mill might have broadened his definition of capital, not only without any loss of precision, but with positive advantage to the clearness of terminology. By so doing, also, he might have brought his definition into harmony with the common, and we think most legitimate, meaning of the term. Instead of defining Capital as goods or property which either are or are not capital according to the intention of their possessor to employ them in reproduction,* he would have done better to define it as reserve-wealth in any form—(all reserve-wealth being obviously available for the employment of labour, even if not actually

* "Reproduction" is itself a very vague term; no two writers agree as to its practical application. A literary friend of mine even maintains, and with a good show of reasoning, that the money spent by Coleridge and De Quincey on opium was a "reproductive" expenditure, since it gave birth to those masterly as well as brilliant literary productions which made an income for those authors, as well as instructed and delighted the world.

so employed): dividing it into "active" or "inactive" capital, according as it is employed in industry or hoarded by its possessors. Let us take an illustration from the recent history of France. In 1850, as in former years, a large amount of realised wealth in the form of the precious metals was hoarded in France,—each man keeping his little store of reserve-wealth in specie in his strong-box. This was national capital in an inactive form. Under the Empire, however, partly by means of Government loans, still more owing to the impetus given to financial and industrial enterprise, a very large proportion of the specie so hoarded has been invested in business: it has become active capital. *Quoad* this amount, the capital of France has not actually increased, but the result has been equivalent to an increase; for a greater part of this amount, formerly hoarded, has become active, effective, reproductive. According to Mr Mill, this is an actual increase of capital; according to our view, it is simply a conversion of capital from an inactive condition into one of activity and reproduction.

The meaning which we would attach to Capital accords very closely with the sense in which the word is used by practical men, and also, we may say, by the general public. By "capital" we mean reserve-wealth,—the amount of property in an *exchangeable* form, and therefore possessed of Value, which is held in reserve by a nation or by an individual. The capital or reserve-wealth of a country consists in the amount of commodities, whether of home or foreign production (including specie), which it holds at any

given time, but does not use for its own consumption; and also in the amount of international currency, in the form of foreign bills or bonds, which the nation holds in excess of the amount of its contemporaneous debts to other countries. The capital of an individual, in like manner, consists in the amount of property which he possesses but does not himself make use of. It matters little in what form that surplus wealth is held. Any kind of wealth is exchangeable into other kinds. So that it possesses Value—*i.e.*, is exchangeable—any kind of property held in reserve by its possessor is capital. What is capital to an individual, it is true, may not be a substantial addition to the national capital. If a man holds a bond upon another man or upon a Government, that is capital *quoad* himself; but whether this bond is capital as regards the country to which he belongs, depends upon the parties to whom he has lent his money or goods. If he has lent these to his own Government, or to a fellow-countryman, the bond does not form any part of the national capital,—for it simply represents goods or money in the keeping of another member of the same community: it has no effect upon the debtor and creditor account of his country with other countries: it simply represents an amount of capital temporarily in the possession of another member of the same community. If all the Home bills and bonds and bank-notes of a country were destroyed, the amount (though not the potency*) of the capital of that country would remain undiminished. But if the bills and bonds which

* See Chapter VII.

that country held upon other countries were likewise destroyed, an equal amount of that country's capital would perish.

Our definition of Capital, therefore, is Reserve-wealth —property of any kind which is available for the employment of labour, whether actually so employed or not. Capital, it is true, may be used in a much wider sense —namely, as including realised wealth of all kinds, whether employed by its owner for his own use or not: and it is obvious that a considerable portion of such property can at any time be converted into capital pure (*i. e.*, reserve-wealth), simply by the owner reducing his "consumption;" whereby a portion of the property, whether land or goods, which a man previously kept for his own use, becomes to him reserve-wealth, which can be lent to others, or employed by its owner in trade. But in this work the word is used simply to signify RESERVE-WEALTH. This is our generic definition of Capital.

At the same time it is to be noted that there is a peculiar quality, the presence or absence of which renders reserve-wealth more or less fully entitled to the name of Capital. Reserve-wealth is usually kept for the purpose of lending to others, or of being employed in trade by its owner: accordingly, it is usually kept in a form suitable for this purpose—*i. e.*, in a form more than ordinarily exchangeable or negotiable. Hence, as a secondary and further, though less generic, definition, we may define Capital as Reserve-wealth "mobilised."

In this secondary and subordinate definition, as in the former one, we are substantially in accord with

the meaning attached to the term by practical men and by the general community. Land, as well as a stock of gold and silver, may be capital; but mark how general usage, by drawing a distinction between these two kinds of wealth, accords with our secondary definition. The remark is often heard that a landowner has not capital to work his estate. According to our primary and generic definition, land and money may be alike capital; but according to our secondary and narrower definition, capital is more especially wealth or property in a mobilised form. And this is exactly the cause of the distinction which is implied in the above remark, that a man has not capital to work his land. By selling a portion of his estate—it may be, waste ground which he has never used—a landowner can obtain money wherewith to work the remainder. In so doing he mobilises one part of his property in order to render more productive the other part. Thus, although both land and money may alike be capital, they are not *equally* capital. For, as the chief use of reserve-wealth is that it may be lent to others, or employed in business by its owner, it follows that such property attains its most perfect condition when it is kept in the form most readily negotiable or exchangeable.

Thus, although all kinds of property may be "capital," or reserve-wealth, that kind of property is more especially capital which is mobilised, or kept in a form the most transferable and exchangeable. Hence, speaking roundly, the capital of individuals comprises a great variety of commodities, which, if classed according to

their exchangeability, or efficiency as Capital, would have Land or a Railway at one end of the series, and Money at the other.

But something more remains to be said. Capital must be considered with regard to its potency as well as to its form and quantity. Just as we have seen, in the case of France, that the amount of capital, or reserve-wealth, in a country forms no criterion of the reproductive effects of that capital—these effects being dependent simply on the amount (not hoarded or inactive, but) in a state of activity: so also is it true that the amount of capital in an active state (*i.e.*, actually employed in production) is by no means a criterion of its reproductive power. We have said that all the bank-notes, commercial bills, and financial bonds in a country—in so far as these are held against members of the same community—might be destroyed, and yet the amount of the national capital remain the same as before; but it is not less true that in such a case there would be a great loss to the community, owing to a diminution in the reproductive power of its capital. The amount of capital, whether held by a nation or by an individual, may remain the same, and yet its reproductive effects may be vastly increased. We all know how a man's capital may be largely augmented in potency by the use of bills and other forms of credit,—as has been fully shown in the opening chapter of this work: indeed, but for this process, our country could not carry on anything like its present amount of trade, or make anything like its present amount of profits.

The yearly increase of wealth in the United Kingdom is dependent upon our economy of capital: it does not depend merely on the amount of goods, land, houses, and suchlike kinds of property, but upon the potency which we impart to such property as a means of carrying on the national industry.

This is the key to our national progress. It constitutes the chief agent in the augmentation of the material prosperity and social wellbeing of our country. A given amount of capital, or reserve-wealth, is by no means a correct index of national progress. The use which is made of that capital, the extent to which it is rendered effective for production, is as important as its quantity. The same amount of reserve-wealth, in short, may produce widely different results.

To sum up. All reserve-wealth—all property not consumed or made use of by its owner—is Capital. But the effect of that capital upon the wellbeing of its owner, or of the community, or of the world at large, depends (1) upon the amount of it which is employed in profitable industry; and (2) upon the economy of the methods by which it is so employed. Every economy in the method of employing capital is equivalent, in its practical effects, to an increase in the amount of that capital. And thus we are brought to the consideration of the most interesting and important problem in economic science,—namely, the Potency of Capital: a subject which we shall elucidate in the chapters immediately following.

VI.

THE ECONOMY OF FORCE

THE peculiar feature of Civilisation—of that development of the higher powers of man which is ennobling and beautifying the world, and the principle upon which all this rich progress depends, consists in the attainment of two opposite and apparently incompatible results. Production must increase, while the Labour of production must diminish. As a prerequisite, or at least as an accompaniment and adjuvant of Civilisation, the amount of production (the supply of the necessaries and luxuries of life) must increase in greater proportion than population increases. The same amount of population must possess a greater supply of the food which ministers to physical development, and of the luxuries which are the handmaid of refinement and of spiritual (moral and intellectual) development. But a mere increase of production goes for little: in fact, an increase of production, when accompanied by an equal increase of human labour, instead of being an adjuvant of civilisation, may

be rather, in its effects, a return towards barbarism,—in which state, undoubtedly, men perform the greatest amount of labour with the smallest amount of profit; as when the savage obtains fire by the friction of dry wood, and his food by following the wild animals of the forest and the prairie.

If it is to be an auxiliary of Civilisation, the increase of production must be attained without an increase of human labour. In truth, if civilisation is not to be confined to the few at the expense of the many—if it is to be a blessing to all, and not a boon to the few and a curse to the many,—increase of production must be accompanied by an actual diminution in the amount of bodily labour. A Society is conceivable in which, by the establishment of slavery, a small class may raise itself into civilisation by means of exacting increased labour from the rest of the community: a civilised oligarchy may establish itself, while the condition of the mass of the community is actually depressed. An increase of bodily labour, of daily physical toil, is incompatible with the development of the higher faculties of our nature. Beyond a certain point, bodily exertion serves directly to enfeeble the intellect, and also the moral instincts. An increased exertion of physical effort, or, what comes to the same thing, a prolongation of the hours of labour, diminishes the intelligence of the workers, and would end by reducing man to the level of the brutes. Hence, the increase of production, if it is to give birth to human progress and civilisation, must be accompanied by an actual diminution in the amount of material toil requisite for that production.

How are these apparently incompatible results attained? By what means is it that Production is increased while bodily Labour is diminished? The answer to this question, the solution of this mystery, gives a key to the true nature of Civilisation—to the real cause of human progress: it reveals the real basis upon which the glorious fabric of human development, alike moral and intellectual, has been reared, and by an extension of which the blessings of Civilisation may be heightened where they exist, and extended to other sections of mankind to whom as yet they are comparatively unknown.

It is the Mind, the understanding and intellectual imagination—the "Promethean spark," that God-given power of Thought, and of generating new ideas, which is the special characteristic of Man — that accomplishes this result. The amount of Force, of productive power, in the world is incalculable, inconceivable; and it is the application of man's intelligence to the manifold forces, or sources of power, around him which enables him almost indefinitely to increase his own power without a corresponding exertion of bodily labour. He masters the other forces, and applies them to his own use. He investigates their properties, and discovers the means of using them. He subjugates and domesticates the animals; he finds out the properties of the vegetable and mineral kingdoms; he investigates the secret and latent forces of nature, and, by discovering their laws or modes of action, he learns to turn them to account, and enlists them in his service. This process, this mastery of the almost infinite sources

of power external to man, is far from complete,—it is but in its infancy as compared with what it will be in future ages: but even now its efficacy, in adding to the powers of man, and hence as a means of civilisation — as a means of increasing production with a diminution of bodily labour — is one of the greatest marvels of human progress. The power of man is already increased immeasurably beyond the force which is inherent in himself. And the result is the same as if human force had experienced an extraordinary development. One man is now equal in productive power to ten or twenty men in earlier times. To multiply the potency of a thing is practically the same as to multiply the thing itself,—indeed, in many cases, it is very much better.

At the present day we are surrounded on all sides by examples of the increased power which man has acquired by the mastery and employment of forces extraneous to himself. Perhaps the best of all examples, for the purposes of illustration, is that of the steam-engine in the form of the locomotive. Forty years ago, as M. Chevalier states,* there was not a single locomotive in Europe; at the present day there are 16,500. The increase of human power thus accomplished is enormous. A powerful locomotive, on a railway, suffices to draw fully 700 tons besides its own weight. To draw a similar weight or mass upon a highway would require 700 horses. Moreover, a locomotive continues efficient

* *Discours prononcé au Collége de France à l'ouverture du Cours d'Economie Politique, le* 18 *Decembre* 1866. Par M. Michel Chevalier, Membre de l'Institut, &c.

for a longer time than a horse; and also it is of superior service, inasmuch as it moves faster than horses could do if used in its stead. Taking all these things into account, M. Chevalier (himself an accomplished engineer) estimates the tractile value of a powerful locomotive as equal to that of 1400 horses. "Supposing, then, that the 16,500 locomotives in Europe were equal only, on the average, to one-third of the power above-stated [*i. e.*, that each locomotive were equal in efficiency to 466 horses], they would represent 7,700,000 horses,—which would be equivalent to the muscular power of 38½ millions of adult and healthy men." And as such men constitute barely a fifth of the population, it follows that the addition made to human force by the use of locomotives in Europe is the same as if the population of our Continent had increased to the extent of 200 millions during the last forty years. And if we take into account the vast number of steam-engines in use otherwise than as locomotives, it is not beyond the truth to say that the power of man in Europe has been trebled during a single generation by the appliance of steam-power alone. As a question of bodily power, the result is the same as if the population of Europe had been trebled; but as regards Civilisation, the result is immeasurably superior,—for the productive force of mankind has been increased without any addition to the requirements of produce for the simple sustenance of life.

Next, considering the question simply as one of economical science, let us observe how this multiplication of Power is effected. As we have seen, a multipli-

cation of material power has been effected without any increased expenditure of Labour, or of the Capital which pays for that Labour. But in what way is this multiplication of force, this economy of human power, effected? Let us again take the steam-engine as an example, and see how human intelligence economises the results of human labour. A mere alteration in the form of the boiler, and of the mode of applying the steam, may suffice to double the power of the machine. An improved form of boiler serves, from the same quantity of fuel and water, to generate within a given time a greater quantity of steam; and the same quantity of steam, by an improved mode of treating it, acquires a vastly increased potency as a motive force. Fifteen or twenty years ago, 7 lb. of coal per hour were needed in steam-navigation to produce a single horse-power; but now the same amount of power is evolved from less than one-half that quantity of coal. The cost of construction of the engines remains virtually the same, and so does their power, yet the cost of working them is diminished one-half. Hence the same amount of Labour, and the same amount of Capital expended in payment of that labour, now suffice to produce a result twice as great as was the case twenty years ago. The result in fact, as regards the expenditure alike of Labour and of Capital, is the same as if every engine had, as regards the power which it evolves, become two engines of equal power. With the same amount of iron and other metals, and with the same amount of labour in the construction of the machine,—with the same quantity of coal to generate the steam, and of attendants to work the machine,

—a locomotive now possesses a potency twice as great as before. The intrinsic value (using that phrase to express the cost of production) remaining the same, the productive power of the machine is doubled.

This result has been accomplished within the last twenty years. But, we need hardly say, since the first invention of locomotives, the economy of force which human ingenuity has effected is very much greater. The highest steam-pressure which Watt attained was 12 lb. on the square inch; at present the force developed is ten times as great, or 120 lb. on the square inch. In 1829, the most powerful locomotive that could be constructed (the "Rocket") could only draw three times its own weight, at a speed of 15 miles an hour; at present, a powerful locomotive will draw ten times its own weight, at a rate of 20 miles an hour. During the same period, the quantity of fuel required for generating a given amount of steam has been diminished five-sixths: in other words, one pound of coal now suffices to develop as much force as six pounds did forty years ago. We may add that, by engineering science, the locomotive has during the same period been gradually improved so as to overcome the difficulties presented by gradients of 1 in 100, 1 in 50, 1 in 25, and 1 in 12, combined with curves of from 30 chains down to 15, 10, 5, and even 2 chains radius: thereby rendering it possible to construct railroads in localities hitherto impracticable, and thus extending the economy of power effected by steam-locomotion.

The same truth is exemplified in a thousand forms around us. This, in short, is what M. Chevalier rightly

calls the "mystery of Civilisation,"—namely, that the same amount of productive force, and of actual production, is nowadays attained by an immensely diminished employment of labour. In truth the prime feature, and the grandest triumph of Civilisation, is, that from the same amount of intrinsic value (*i. e.*, with the same cost of production*) we obtain, from generation to generation, a steadily increasing amount of effective or productive power. The intrinsic value of a thing remaining the same, the thing is made, by human intelligence, to possess a constantly increasing effective value as a means of production—as a means of augmenting the results of human labour, and of carrying on trade and industrial production of all kinds as effectually as before, with an ever-decreasing cost. This is truly the mystery, the marvel, the triumph of Civilisation. It is worthy of exposition of itself: it is a theme worthy of the pen of a philosophical historian: it is the peculiar feature, and most powerful auxiliary, of human progress. But it is not for this purpose only that we call attention to it. In the next chapter, we shall give to these remarks a highly practical application.

* "Intrinsic value" may have a wider meaning than the "cost of production." For example, in the case of some of the products of the earth, such as the date-palm and its fruit, there may be no cost of production at all, and yet the fruit possesses intrinsic or inherent value. But in this chapter, and wherever else the word occurs in this book, it is used exclusively with respect to objects like specie or locomotives: and it designates the cost of production, or amount of labour expended in production (which is the only kind of intrinsic value which such articles can or do possess), in contradistinction to the "effective value," or the practical efficiency of the object in fulfilling the purpose for which labour was expended upon it.

VII.

THE POTENCY OF CAPITAL

THE two greatest auxiliaries or handmaids of Production are Roads and Money. Neither of these, of themselves, produce the necessaries of life: on the contrary, primarily they effect a withdrawal of labour and material from the production of the necessaries and fundamental requirements of human existence. Roads occupy a portion of the land available for supplying the wants of the population. Their construction also absorbs an amount of labour which otherwise might be directly applied to cultivation and other forms of production. In the case of Money in the form of specie, a similar withdrawal of labour takes place from the production of the first requisites of life. But in both cases this primary waste, so to speak, is far more than compensated by the resultant economy. Although neither roads nor money are of themselves directly productive—although indeed they actually, at the outset, constitute an obstruction or absorption of the means of production,—nevertheless,

they multiply immensely the Force available for production. They add nothing to the amount of food or clothing or houses, requisite for the support and comfort of life, but they vastly augment the power possessed by man for the production of these and all other commodities. They enable a given amount of human power to effect an immense increase of production.

For example, by means of a road or highway, a farmer can bring to his farm the manures and implements which he requires more easily, and therefore at less cost, than before; so that the cost of cultivation is diminished: he can raise the same amount of produce with a diminished outlay,—or, which is the same thing, with no increase of expenditure he can raise a greater quantity of produce. Again, by means of roads, the farmer can send his produce to market at less cost than before: and consequently he can afford to sell his produce (supply food to the community) at a reduced price. Thus, by means of roads, the price of goods is diminished in two ways: firstly, by a reduction in the cost of production, and secondly, by a reduction in the cost of conveying the produce to market. In the case of a simple exchange of goods, the economy is equally manifest. If a man exchanges a portion of his goods, say cattle or grain, for the goods of some other man, say coal or lime or iron, the cost of conveying these goods from the one man to the other, and the time lost in the transfer, constitute an expense upon the transaction,—an obstacle to that exchange of goods which is indispensable to mankind at all times, and peculiarly so in a civilised community Roads, by lessening the cost and increasing the rapidity

of conveyance, greatly facilitate such transactions. In short, they add alike to the power of production, and to the means of exchanging the goods so produced. At the same time, as all commodities in transit or in store are inactive—as they are wealth in a form temporarily unproductive—roads effect a great economy of capital: they enable a given amount of capital to support a larger amount of trade.*

* By overlooking these facts, a serious error has been committed by some eminent authorities in the science of finance. For example, it has been regarded as an axiom that the construction of railways in this country tends to turn the Balance of Trade against us. The argument is as follows:—The construction of railways, by occasioning an increased expenditure in wages, leads to an increased consumption of the necessaries and luxuries of life in this country; and, as a large portion of the articles so consumed come from foreign countries, this necessarily increases our Imports. If the capital so expended on railways were invested in the production of goods which could be exported, the increased consumption—*i. e.*, the increase of Imports—would be balanced by a simultaneous increase of our Exports. But as the construction of railways does not produce any goods which can be exported, the increased consumption attendant upon their construction occasions an unusual excess of our Imports over our Exports.

But the construction of railways, as a question of fact, occasions no withdrawal of capital from the production of goods for export—it usually takes place simultaneously with the ordinary increase of capital invested in such industry: so that any embarrassment could be only of an infinitesimal kind. Moreover—and this is the cardinal point of the question—the effect of railways and also of telegraphs is alike to economise our Imports and to augment our Exports. For example: say that it took six days to transport heavy goods from London to Liverpool, or any similar distance, and that by means of railways the distance could be traversed in a single day. The consequence would be, that merchants or manufacturers, instead of having to keep a week's stock of goods in hand, could lessen this stock to a single day's supply. Hence the amount of imported goods on hand would be reduced five-sixths. With regard to wholesale merchants for the home-trade, the result would be the same. So that a very large portion of goods previously inactive—whether imported produce or goods designed for export—would be economised and rendered effective:

Money serves exactly the same purpose as roads do. This parallel was noticed a hundred years ago by Adam Smith; and it not only still holds good, but nowadays furnishes a richness of illustration far beyond what was possible in the days of the eminent Father or Founder of the science of Political Economy.

In early times, so far back as 2000 years ago, civilised communities perceived that the system of barter opposed so many obstacles to the free exchange of goods, which is a requisite of civilisation, that it was advantageous for them to devote a portion of their wealth or labour to supply themselves with Money, in the form of the precious metals, in order to facilitate production and all the other industrial transactions of life. This was precisely equivalent to the making of roads. It facilitated the transfer of property from man to man—the locomotion of Value,—just as roads facilitate the transfer of commodities from one place to another. Since then, Civilisation has done with Money exactly what it has done with Roads. As we have seen, the effective power of roads has been multiplied enormously by the adoption of the steam-locomotive; and the power of the locomotive itself has been vastly increased, without any increase of bodily labour, by the application of human intelligence to its construction. The intrinsic value (*i. e.*, the cost of production) of the machine remaining the same, its effective power has been doubled even within the last twenty years. And a similar economy

the result being a more rapid return of the capital invested in trade and commerce,—so that the same amount of trade and consumption could be carried on with less capital than before.

(or, which comes to the same thing, a similar multiplication) of power is still being carried on, and is yearly accomplishing greater results.

Thus, while multiplying Production without any increased expenditure of Labour, human intelligence has in like manner lessened the cost of the means by which Wealth is applied to production—in other words, by which labour is paid for. Civilised communities advanced from the cumbrous system of payments in kind to payments in metallic money; from that they have advanced to the banking-system and paper-money, supplemented by commercial currency in the form of bills. The principle in this case is the same as that which has aided human progress in material industry. Man has multiplied the potency of his material agents, without increasing the expenditure of labour in their production: he has multiplied their effective power or practical value without adding to their intrinsic value. And this, we repeat, is the cardinal feature of Civilisation—the indispensable requisite to human progress, and to the increase of human comfort and wellbeing.

Things which are in one respect equal to the same thing, are in that respect equal to one another. As soon as coins, by common agreement or by legal enactment, came to possess the same exchangeable value as sheep and oxen, they became in that respect as valuable as sheep and oxen were. Unlike sheep and cattle, coins possess no value as food, but they soon became superior to these commodities in exchangeable value—as a means of conducting the exchanges of property by which not only all trade, but also the daily "consumption" of

a community, are carried on. They were not food or clothing or any of the necessaries of life, but they were convertible into those necessaries, and also into any other kind of property, or into labour or any of its products, whether material or intellectual.

The principle of Money, and also of Banking, is simply this: that if a man can get a thing when he wants it, the effect is the same as if he always had it. Banking, which has given such an impetus to Civilisation, to the wellbeing of mankind, owes its value entirely to the multiplication of power which it confers upon the commodity (money) in which it deals. Banking makes no addition to the amount of coins in a country, but it vastly increases their potency. Hence the practical effect of banking is the same as if the amount of coins in a country were greatly augmented. The man who deposits his coin in bank has it at his command as much as if he kept it in his own house; and yet, nearly the whole of the amount is contemporaneously in the possession of others, who actually employ it. The coin is at the free disposal of its owner, yet simultaneously it is being used by others. It thereby acquires a vastly increased potency. Just as the same quantity of fuel in a locomotive can by human ingenuity, and at no extra cost, be made to produce a double amount of motive power,—or as the vapour generated in the boiler can be similarly increased in potency; so does a given amount of coin become, by means of banking, immensely multiplied as a motive power of industry,—which is the special use of Money, just as propelling-power constitutes the special function of the locomotive. In the one case as

in the other, although there is no increase in the cost of producing them, the effect is the same as if the auxiliaries of production (whether coins or locomotives) in a country were numerically increased.

The same feature and fundamental principle of civilisation is observable in the economy effected by the use of Paper-currency, in all its forms. Just as coins became equal in exchangeable value to sheep and oxen as soon as they became equally convertible as these into commodities of all kinds; so is paper-money equal in exchangeable value to coin when it is convertible into coin, and therefore equally convertible as it into other commodities. In like manner, commercial bills, within their own sphere, are equal to notes or coin, because convertible into them; and although not designed or fitted for general circulation, like banking-currency, bills in point of fact have a wider circulation than either coin or bank-notes, being preferable to either as a means of transmitting Value from one country to another. In truth, owing to this superiority, good bills are at a premium compared to coin or specie: *i.e.*, a foreign bill for £1000 usually brings a higher price than 1000 sovereigns.

The great triumph of Civilisation, or human progress, is to attain equal results by a less expenditure of labour. And when paper-money serves the same purpose as coin, the fact that it costs less than coin, so far from being a disparagement of it, constitutes its special recommendation. The exchangeable value of currency, as indeed of everything, constitutes its actual value. The cost of production is a subsidiary point. No one will

pay more for an article merely because more labour has been employed in its production. If two locomotives be equally effective, their exchangeable value is the same,—howsoever great a difference there may have been in the cost of constructing them. In like manner, when a man can buy as much with a bank-note as with a sovereign, it does not matter to him that the intrinsic value (*i. e.*, cost of production) of the one is greater than that of the other. When Paper-money has the same purchasing power or exchangeable value as coin, it is equal to coin as currency: just as coin, from the same cause, became equal in exchange-transactions to commodities which are the necessaries of life. The value of a Locomotive, as a locomotive, does not depend upon the cost of its construction, but upon the amount of its motive power. In like manner the value of Money, as currency, does not depend upon the cost of producing it, but upon the purchasing power which it possesses.

It would be too absurd to enact that a steam-engine of a given amount of horse-power should always represent an equal amount of labour expended in its production. This would be downright barbarism,—a reversal of the principle, and a check to the progress, of civilisation. But it is equally a check upon civilisation and upon the wellbeing of a community, to enact that no addition shall be made to the currency of a country, unless the same amount of Money shall represent as much labour as was necessary for its production two centuries ago. To say that money produced at a less cost than was requisite in the seventeenth century, before the

establishment of banking and banking-currency, cannot possess the same purchasing power, is quite as absurd as to maintain that a locomotive of the present day cannot possess double the amount of motive power possessed by one constructed at the same cost forty years ago. If Civilisation and the national wellbeing are to obtain a full and free development—if they are to progress in the future as they have done in the past—it is indispensable that this fundamental principle of Civilisation be adhered to, and that the same economy be practised in the means of exchanging commodities as in the means of producing them: the same economy of force, or of intrinsic value, must be developed in the appliance of Capital as in the employment of Labour.

Continuing our elucidation of what, in brief, we have called the Potency of capital, let us take a simple case —but one which, from its social bearings, has excited much controversy:—The same amount of capital is more potent, is more available for the production of wealth, when concentrated in the hands of a few than when diffused among many possessors. It is so for two reasons. Firstly, because a few large capitalists are more certain to possess the intelligence and enterprise requisite for an efficient employment of their reserve-wealth than a large number of small capitalists are; and secondly, wealth when in the hands of a few, is more readily available for productive industry than when dispersed over the community at large. Hence the prevalent opinion among political economists, that it is best to have the wealth of a country concentrated in the hands of a comparatively small number of possessors. On the other

hand, as regards the moral and social condition of a nation, it is better that wealth should be widely diffused —in other words, that no chasm should separate the multitude from the few; that vast wealth on the part of a few should not coexist with depths of poverty and want on the part of the many. True it is that in the former case there may actually be more employment for labour than in the latter; but it is not less true that the possession of property has an elevating effect upon men far superior to that which arises merely from the receipt of high wages.

Hence two rival Schools have arisen,—the one maintaining that it is better to have the wealth of a country concentrated in a few hands, the other advocating a system of small proprietors or capitalists. In great part—as happens in most abstract discussions—this is a difference of terms rather than a substantial divergence of opinion. The one school—which regards the matter from a Financial point of view—maintains that since wealth is most effective when held by a few, the result must be that the wellbeing of the nation is more promoted in this fashion than the other; in other words, that, with a class of large capitalists, the general wellbeing of the community, the increase of wealth among all classes of the nation, is more rapidly promoted than if the bulk of the national wealth were widely diffused. This school looks chiefly, if not solely, at the process of wealth-making. The other school—which regards the question from a Social point of view—errs by desiring the end, without a proper regard for the means by which that end is attainable. They desire—as all philanthropists and social reformers must

desire — to banish poverty, and its usual accompaniments, ignorance and crime, from the mass of the community; and as the possession of property is the chief cure for such evils, and gives a man a degree of self-respect greater than that which arises from the mere receipt of weekly wages, they are in favour of any system which tends to diffuse the possession of property among the community at large. Their desire is good; but they overlook the fact that the only legitimate way of putting the masses in possession of property or realised wealth is by securing for them a higher pay for their labour. And it is obvious that, the amount of national wealth remaining the same, the rate of wages will be highest under the system which gives to that amount of wealth the highest amount of potency,—in other words, which renders a given amount of wealth efficient for the production of the greatest results.

Hence, ugly as the doctrine of the Economists looks at first sight, and to superficial observers, it is really true that (*cæteris paribus*) it is best for the material interests of a country when the bulk of its reserve-wealth is in comparatively few hands; because, in such a case, the potency of that capital is greater than if the same amount of wealth were dispersed among very many possessors.

Fortunately, Civilisation has given birth to a system which, to a great degree, reconciles the two opposite systems. Banking, when fully developed in a community, unites the objects which each of these rival schools has at heart. By means of banking, a given amount of wealth acquires nearly the same potency

when diffused among millions as if concentrated in a few hands. Banks take the place of large capitalists: they gather into one fund the small savings or reserve-wealth of the masses, and thus render these as available for the employment of labour as if they belonged to a single possessor. And also, banks supply the knowledge and enterprise requisite for the employment of that wealth, which is in great part wanting on the part of the actual owners of it. Hence the banking system accomplishes the same result as if the wealth of a country were concentrated in the hands of a few large capitalists, and yet allows of that wealth being actually diffused among tens of thousands of owners. The banking system, in short, immensely increases that potency of capital of which we have spoken above, and which has quite as much to do with national progress and well-being as the actual amount of the national wealth.

Banks, we repeat, take the place of large capitalists: so that the money expended by the wealthy and enterprising portion of the community in trade or industrial works, such as railways, &c., although dispersed in wage-payments among the labouring classes, who do not themselves employ the money thus acquired in reproductive industry, is not thereby withdrawn from production,—seeing that it immediately finds its way back into the banks, who employ it just as a large capitalist would. If there were no banks, a large portion of the money expended in the construction of a railway would stagnate as small hoards in the hands of thousands of owners,—a very long period would elapse before it became again available for production by returning into

the hands of large capitalists: whereas, through the agency of banks, the small sums are quickly reunited, and become disposable anew for industrial investment. In this way capital is re-collected as soon as dispersed: and hence, by means of Banking, the reserve-wealth of a country, although ceaselessly dispersed in industrial expenditure, practically remains massed, or concentrated in comparatively few hands, and therefore in the most effective condition for augmenting production.

In this way a very large amount of capital which would otherwise become "fixed," in consequence of its being employed in industrial enterprise, immediately reappears as "floating" capital, available for similar investment by other parties. But before treating this point in detail, we have to show the important part which Banks, in unison with the operations of Finance, play in increasing the potency of capital by rendering *negotiable*, or readily convertible into money, very many kinds of property which otherwise would be wealth only in a "fixed" form,—*i. e.*, yielding interest to its owner, but not convertible into money at his pleasure.

VIII.

NEGOTIABILITY OF VALUE

By Negotiability, we mean the power of converting a commodity, or property of any kind, into Money. The various forms of Property differ greatly as regards their negotiability,—some of them being readily convertible, by sale or loan, into money, and others not. Corn, cotton, coal, and iron, for example, are naturally more convertible into money than diamonds are, because there is a wider and steadier demand or requirement for the former articles than for the latter. A large estate, also, is less readily negotiable than a stock of corn or cotton: partly because it is not so divisible into small portions, also because the science of Finance has not as yet been so fully applied to landed property as to merchandise.

Any process which increases the negotiability of a commodity, thereby increases its value. The intrinsic value of the commodity (the cost of its production) is not thereby augmented, but its exchange-

able value is: and it is the exchangeable value of anything—*i. e.*, the faculty of being converted into other commodities—which constitutes its actual value. Land, for example, acquires no additional fertility by being rendered more readily convertible into money,—it will not grow a single bushel more of corn, or support an additional ox or sheep; nevertheless its effective value is augmented by the process, inasmuch as its intrinsic value becomes more fully and freely at the disposal of its owner. A man will give more money for a commodity which he can at pleasure reconvert into money than for another of equal intrinsic value (*i. e.*, whose cost of production is the same) which is not readily convertible. And for this good reason, that in the former case he is at all times sure of getting ready value for his property,—of getting that value reconverted into money; whereas in the latter case, if he is compelled suddenly to convert his property into money, the probability is that he will have to submit to accept less than its intrinsic value in order to find a purchaser.

This is the state of the case as regards Individuals. From a National point of view, the advantage of increasing the negotiability of property of all kinds is equally conspicuous. We have seen the vast economy of national capital which Banking effects: and the larger the amount of property brought within the sphere of banking operations, the greater is the economy,—in other words, the more potent for reproduction does the national wealth become. A man who keeps his reserve-wealth in bank, as we have pointed out, has the full use of it, while at the same time nearly the whole of

the amount is in use by others. The effect, therefore, is the same as if the capital were multiplied,—as if it were in two places, or rather in the hands of two individuals, at the same time. Mr Mill says that if a thousand pounds belonging to A be lent to B, it is as much capital to B as if it belonged to him; while A is as rich as before, since he has a lien on B's property which he can sell for the amount. This is true in principle; but it is obvious that the value of A's bond depends greatly upon the negotiability of that bond.

Now, by what means, and on what principle, can this quality of negotiability be imparted to, or increased as regards, commodities or property of any kind? In order to show this point clearly, it is necessary to observe what is the fundamental basis of exchangeable value in its most perfect form,—namely, in the form of money, or of currency of any kind. What is the essential element to which Currency of all kinds owes its value? It is the knowledge that this particular thing (currency) will be generally accepted in exchange for other kinds of property. There are various kinds of currency in the world, but each owes its value to the same cause,—namely, that it is exchangeable into the other kinds of currency, and also into all kinds of property. And that kind of currency which most fully possesses this exchangeability, is the most perfect.

This element of value was not at first possessed even by the precious metals. In the form of bullion, gold and silver are a most imperfect kind of currency even at the present day. And in early times, when money

first began to take the place of barter, a man was slow to accept coins in exchange for his goods, being uncertain whether or not the other members of the community would do the like. Still more was he doubtful whether the coins which he was offered for his sheep or oxen would suffice to procure for him (*cæteris paribus*) the same number of sheep or oxen when he wanted them. A Government decree was needed to make this sure —or at least was the most potent means of doing so,— by announcing that the State was ready to accept in payment of tribute so many of those coins in lieu of so many sheep or oxen, or of other payments-in-kind. As soon as the Government gave this guarantee for the value of the coins, they became generally exchangeable.

Just so is it with all other kinds of currency. A commodity must have an adequate *extrinsic* guarantee of its value as a medium of exchange—it must have an extraneous value added to or superimposed upon its intrinsic value—before it can become currency of any kind.

COMMERCIAL CURRENCY.

In considering this matter, let us first take the case of Bills,—which play so important a part in the trading operations of all civilised countries. Upon what basis do bills become commercial currency—the wholesale currency of trade? They represent Value; they are the value of goods converted into a negotiable form. Few men want the goods, but the *value* of the goods, in the form of a bill, is a highly negotiable thing.

Although few persons would accept in payment a cargo of cotton or sugar, many persons will take a negotiable draft embodying the value of the cargo. But before a bill becomes negotiable, there must be some guarantee that the bill does represent a certain value in goods, and, still more, that it will be convertible into money (*i. e.*, paid) at a certain date. In this way, some other party than the drawer of the bill (the seller of the goods) must intervene as a guarantee.

As regards "Foreign" bills. A merchant in Calcutta ships goods to England to the value of £1000, and he draws a bill for that amount upon the merchant to whom the goods are sold or consigned. He pins to this bill of exchange the bill-of-lading (the certificate of the shipment of the goods, to the holder of which alone can the goods be delivered), and takes these to his bank, where his character is known,—and the bank buys (discounts) the bill, giving him the value of it in money. The bank has a twofold security for this loan or purchase *—firstly, the goods which the bill represents, of which the bank gets possession by means of the bill-of-lading; secondly, the general estate of the drawer, which is liable to the bank in the event of the bill not being duly met (*i. e.*, paid at the specified date) by the merchant in England upon whom it is drawn, and to whom the goods have been consigned. The bank then endorses the bill; and the bill, thus guaranteed by the bank, becomes effective commercial currency. Some customer of the bank, who has to send £1000 to Eng-

* To discount a bill is really to purchase it, taking a warranty of its soundness from the seller—*i. e.*, the person who offers it to the bank.

land, takes this bill from the bank instead of specie, and transmits it by post to his creditor in England; and this person, on receiving the bill, either passes it in payment to some other merchant, or takes it to his bank, where the amount is placed to his credit just as if he had paid-in, or "deposited," the same amount in money of the realm. The sequel of the bill's course is, that in due time the merchant to whom the goods were sent "takes up" the bill (*i. e.*, pays the amount to the bank), gets the bill-of-lading, and therewith possession of the goods.

Such a bill may also circulate without passing through and being endorsed by a bank at all. The drawer, being a person of good credit, may pass the bill (with the bill-of-lading attached) in payment to some other merchant in India, to whom he is well known. This latter endorses the bill, and then has little difficulty in passing it in payment to a third party, who may do likewise. And so the bill may circulate through many hands,—growing more perfect as commercial currency with each successive endorsement; and this, without the bill ever having been formally "accepted" by the merchant in England upon whom it is drawn. The "acceptance" of a bill, in fact, as regards the efficacy of the bond as commercial currency, is important simply as making two parties, instead of one, sureties for payment of the bill; and by passing through several hands, each party endorsing it in succession, a bill becomes of more assured value than if it had been simply drawn and accepted in the ordinary course. A foreign bill upon London occasionally passes through twenty or thirty

hands in successive payments, as currency, before being accepted by the English merchant upon whom it is drawn. We have seen several cases in which a three-months' bill was not presented for acceptance in London until the very day before it became due (*i.e.*, payable in money),—the bill having ceaselessly acted as commercial currency during the interval.

Or take the case of a "Home" bill—*i.e.*, between two merchants in the same country: a bill accepted in the same country where it is drawn. A wholesale merchant sells goods to the value of £1000 to a retail-dealer or shopkeeper, and immediately draws a bill for the amount; the shopkeeper at once "accepts" the bill, —*i.e.*, binds himself to pay the amount in money at the specified date. The wholesale merchant then discounts the bill at his bank, where the amount, minus interest for the time the bill has to run, is placed to his credit, just as if he had paid-in money; or else he uses the bill as currency, giving it in payment to some other merchant, who in turn may pay it away to another, and so on,—the bill increasing in repute as currency, as a medium of exchange, in proportion to the number and quality of the endorsements which it bears.

It is in this way that goods become the basis of a currency suitable for Trade. Merchants of established credit make themselves responsible for payment of the bill, which represents the Value of goods, in money at the specified date. This guarantee is the great element in the negotiability of a bill; it is this which renders bills effective as commercial currency. The value of the goods is actually a subsidiary point: it

is the guarantee for payment of the bill that is the prime, and generally the only, thing considered. A bill which is not drawn upon goods at all—which is simply a promise to pay a certain sum of money at a certain date,—if guaranteed (*i.e.*, drawn, endorsed, or accepted) by persons of well-known credit, is as negotiable as a bill which is drawn upon goods. A merchant who is offered a bill in payment thinks little about the quality and value of the goods upon which the bill may be drawn, or whether any goods are drawn upon at all. The goods drawn upon may be of excellent value, but he does not want the goods,—he wants the *value* represented by the bill; and if there is adequate security for payment of the bill, that is all he cares for. To show how much—in most cases how entirely—the negotiability of a bill depends, not upon the goods upon which it may be drawn, but upon the *guarantee* for its payment, let us take an exceptional case. Suppose Baron Rothschild were to draw a bill upon some person abroad, and were then to send the bill for sale on 'Change, the bill would at once be bought at full value, simply on the credit of the drawer: (1) without reference as to whether it were based upon goods; (2) without being accepted by the party upon whom it was drawn; or (3) without any one caring to inquire as to the credit of the drawee, or even whether there were such a person in existence.

As long as a merchant has only to make the wholesale payments of his trade, this commercial currency is all that he requires. A Calcutta or Paris merchant who holds a bill payable in England, as long as he requires

only to make the wholesale payments of trade, does not or need not take the bill to a bank at all. He sends the bill over to some English creditor of his, and discharges his debt by the bill just as thoroughly as if he had sent payment in specie. Or else he sells the bill to some merchant in his own country who has to make a payment in England, and who thereupon makes this payment by transmitting the bill—or several bills, if more than one be needed to make up the required sum. An English merchant, in fact, often receives in payment from a foreign debtor a bundle of bills, drawn by different persons and in different places, and the debt is thereby discharged without the use of specie or money of any kind.

Such is Commercial Currency. Such is the medium of exchange by which the wholesale operations of Trade are carried on. But merchants, and all classes of the community, have need also of another kind of currency. A bill is of no use in making the ordinary retail payments of life, nor is it very effective even in general payments of any amount beyond the sphere of commercial business. To make these retail and general payments, recourse must be had (apart from the use of metallic money) to Banking Currency.

BANKING CURRENCY.

The conversion of Commercial into Banking currency is accomplished on the same principle as the conversion of the value of goods into commercial currency. Bills

become a basis of banking currency, just as goods are made a basis of commercial currency. In either case there must be superimposed or added to this basis a *guarantee of value*, such as will be considered adequate and ample by the class or community among whom the currency is meant to circulate.

A merchant who requires general currency, effective for payments of all kinds in his own country, takes some of his commercial currency (*i. e.*, bills) to a bank, and obtains in exchange banking currency — bank-notes. These Notes represent the value of the Bills, just as Bills represent the value of Goods. In the case of the Notes, even more than in the case of the Bills, the public do not (practically cannot) inquire as to the commodity whose value is represented: the essential point is that (whatever be the value or commodity in exchange for which the bank has given its notes) payment of the notes on demand is secured by the guarantee of parties of established credit. This guarantee gives to the notes general acceptability: it makes them "currency," effective in payments of all kinds.

This Banking Currency must—in order to fulfil its object as general currency—possess a more unquestionable guarantee, or at least a guarantee whose adequacy is much more widely known, than is requisite in the case of Commercial currency. Commercial bills are a currency meant to circulate within narrow limits—*i. e.*, among a few parties only, who are, or who suppose themselves to be, cognisant of the solvency of the individuals who issue or endorse the bills. Bank-

bills, in the form of notes,* are a currency for general circulation; they pass from hand to hand among persons who in great part cannot be cognisant of the exact position of the issuing bank. Hence the first requirement of banking currency is, that it be issued by powerful Companies, possessing a reserve of wealth amply adequate to insure the value of the notes (bank-bills) which they issue. The second requirement is that, unlike commercial bills (which are not payable till a stated time), bank-notes be always payable in coin of the realm by the issuing bank on demand. Thirdly, bank-notes are issued for smaller sums than commercial bills are: the latter being meant for wholesale operations, while the former are chiefly needed for retail payments. A merchant who is in want of currency for general use takes a trade-bill for £150 to his bank, and thereupon receives in exchange several bank-bills (notes) of small denomination, suitable for retail payments, and acceptable with the public. If, instead of a trade-bill, the merchant had so many pounds of gold or silver bullion, he would need to do likewise if he were in want of general currency. Bullion, in truth, will not circulate so freely as a commercial bill does. A merchant may, indeed, take his bullion to the Mint, and get it converted into coins of the realm, but he finds it much easier to take the bullion to the bank and get banking currency in exchange for it.

Banking currency, in short, is issued in exchange for

* We need not here speak of bank post-bills, which form a very small part of a bank's circulation, and which are not meant, or fitted, to be general currency.

commercial currency, and also in loans upon the deposit with the bank of property of various kinds,—the borrower's whole estate also being liable in repayment. And the currency thus issued circulates freely: (1) from the fact that, in addition to the property in exchange for which the issue is made, the capital and credit of the bank are an adequate guarantee for the value of its bills or notes; (2) that these bank-notes are payable in coins of the realm on demand; and (3) that they are for small as well as large sums, so as to be useful for all purposes. The *rationale* of the process is the same as if a bank were to take a bill based upon goods and guaranteed by two or more good names,—were to endorse that bill, thereby adding the credit of a great financial establishment to the commercial guarantee which the bill already possessed,—and were then to break up the bill into a number of smaller bills, for the convenience of the public, at the same time engaging to pay those bills in coin of the realm whenever the holders of them should desire it. The merchants remain liable to the bank for payment of the bills; and the bank makes itself liable to the public for payment of the notes which it issues in exchange for the bills.

The banks, of course, make a profit on the transaction. In order to insure payment of their notes on demand, they must keep in hand an adequate amount of specie, which yields no interest; and they must be reimbursed for this expense, as well as compensated for the risks of loss which they incur from some of the bills proving bad. These charges, and the cost of the establishment, together constitute the "bank-rate,"—the charge which

a bank makes for discounting bills, or making advances upon other negotiable securities—*i. e.*, for converting these into general currency.

The operations of Banking, and the economy thereby effected, are limited only by the amount of Property existing in a readily negotiable form. As a bank undertakes to repay in money the value of the property which it accepts in deposit, it must take care that the property so deposited is of a kind readily convertible into money, and the conversion of which does not necessitate the bank's engaging in business other than its own. Accordingly, banks will not receive in deposit, or lend directly upon, goods of any kind, merchandise, houses or suchlike forms of property: because, if they did so, they would be liable to become merchants. In the event of the loans made upon such securities not being repaid at the specified date, the banks would have to sell the goods, houses, estates, &c., upon which they had given credit; and this would lead them into an entirely different kind of business from their own, and one which they are not fitted to transact successfully.

But if a man sells his goods, or his house, &c., and receives the value in a bill payable at so many weeks after date, his property thereupon assumes a form upon which banks will readily make a loan—or rather an exchange of property,—allowing their customer to draw upon them for the amount either by cheques, or in notes or coin. It is only merchants who want merchandise; but almost any one will take in payment the Value of the merchandise, in a form convertible into money. An

iron-merchant would not accept a cargo of cotton in discharge of a sum due to him; because he does not deal in cotton goods, and has no proper means of disposing of them: but he will accept the Value of that cargo embodied in a negotiable and convertible form,—in a form convertible into money without any business-operation on his part. It is the same with banks. They cannot legitimately make advances upon merchandise; they have no proper means of selling it in the event of their loan upon the merchandise not being repaid at the specified time. But they will willingly lend upon a bill or bond (in other words, the value of certain goods or property guaranteed by a person of good repute whose whole assets are liable in payment), which in a month or three months' time will be converted into money without any action upon their part.

FINANCIAL CURRENCY.

Financial Currency consists of bonds of various kinds, and bearing different names. Like commercial currency, these embody the Value of property, assured not only by the property upon which they are issued, but also by an adequate extraneous guarantee, consisting of the liability of the whole assets of the issuer for payment of the amount of the bond. Financial currency, however, differs from commercial currency in two respects. Firstly, it is issued by Companies instead of by individuals; and, secondly, it possesses a double guarantee compared with Commercial currency,—inasmuch as the latter is issued solely by the individual who pos-

sesses a right to the value of the goods upon which the bond is based, whereas Financial currency possesses not only this basis, but also the credit of the Company who take this bond and endorse it with their own credit.

This extra guarantee is requisite in consequence of the lesser natural negotiability of the property with which financial companies deal, compared with ordinary merchandise. A bill drawn upon the value of so much cotton, corn, or other merchandise, is more negotiable than a bond issued upon houses or land, inasmuch as there is a steadier demand for the former kind of property than for the latter,—in other words, the latter commodities are in ordinary circumstances less saleable at their intrinsic value than the former. Hence an extra guarantee is requisite before bonds upon land, houses, &c., become readily negotiable securities: *i.e.*, securities readily convertible into money, — in other words, securities in exchange for which banks will allow a customer to draw upon them in money, or by cheques, for the amount. Negotiability, in short—*i.e.*, the power of converting property into money—depends upon the readiness of banks to give their currency in exchange for the property in question. And the less negotiable any kind of property is naturally, or in itself, the more potent must be the extraneous guarantee for its value before banks will accept it in exchange for the power of drawing upon them for the amount in money or by cheques. It is the special object of Financial companies to supply this extra guarantee, in order to bring within the sphere of Banking operations many kinds of property which otherwise would be excluded from it.

In accordance with the principle of division of labour,

financial companies may separately devote themselves to distinct kinds of business. One may deal with land, another with houses, another with ships, and so on. But the entire operations of Finance may be typified by the *Credit Foncier* and the *Credit Mobilier*,—the former of these Companies dealing with fixed property in the form of land and houses, and the latter with movable property, in the widest sense of the term. By means of such Companies, a man who suddenly requires to convert a portion of his property of any kind into money, can do so without selling his goods or property, and much more easily than by sale, by giving a bond over them to one of those Companies, and getting it endorsed by the Company (paying a commission on the transaction),—after which he takes the bond to a bank, which in exchange for it will allow him to draw for the amount in money. This is not the precise form of the transaction, but it is the principle: and it is only with the generic nature of the system that we have to do at this stage of our work.

Financial companies are comparatively novel establishments in this country, and it is only natural that some of them should at the outset have made great mistakes. But they are most valuable institutions,—they are a most important addition to our financial system: and it is easy to see that, alike in the extent and in the variety of their operations, they are destined to experience a great development.

Their special function is to increase the negotiable value of all kinds of property,—in other words, to bring many kinds of property within the sphere of banking-

operations which otherwise could not be so included. In fact, to use a homely simile, they are to the banking-system what the art of cookery is to the bodily frame. Just as some kinds of food require no culinary preparation, while others do; so there are some kinds of property naturally possessed of so much exchangeable value that banks will readily deal in them, while others require their exchangeable value to be largely increased before they can be brought within the operations of banking. Comparatively few raw articles are readily assimilated into the human frame—*i.e.*, converted into the circulating fluids which support life; but very many substances can be made available for sustenance by means of culinary science. In like manner, comparatively few forms of property naturally come within the sphere of banking-operations—or, in other words, are readily convertible into the circulating medium requisite to carry on trade and production; but an indefinitely large amount of property in all forms may be rendered convertible by means of the science of Finance. And every triumph of this kind increases the potency of capital, and with it the power of production.

Every extension of this financial economy tends to augment the extent of banking-operations. Finance, in fact, acts as the cook by which commodities are prepared, or rendered suitable, for the operations of Banking, by which their negotiability, or convertibility into general currency, is perfected. This, as has been fully shown in previous chapters, constitutes practically an immense addition to the wealth of a country, by giving an increased potency to the agents of production.

To individuals, the effect of the conjoint operations of Banking and Financial companies is to place their wealth more fully and freely at their disposal, by increasing its convertibility into money, and thereby into any kind of property at pleasure. A man who has invested his money in commodities, or substantial property of most kinds, can now reconvert his property into money to an extent never known before. Suppose he has invested his wealth in a "fixed" form, so that in former times he had command only over the interest or annual profit on the wealth so invested, he can now (speaking roundly) reconvert that wealth at pleasure into a "floating" form by exchanging it into a bank-credit, which enables him to obtain money without having to force a sale of his property. In fact, to take an extreme yet nowadays not unusual case: Suppose a Company, or a few large capitalists, invest a million in the partial construction of a railway —a form of property not at all saleable, the line not being completed, and no returns obtainable on it: nevertheless, by giving a bond over the line to a Finance Company, they can get a large portion of the capital so invested returned to them—and this they can devote to the completion of the railway.

By such processes, the old distinction between "fixed" and "floating" capital—even as regards the correct use of these terms—has to a great extent disappeared; and an immense addition has thereby been made to the potency of capital, and consequently to the agents or *media* of employment and production which constitute the basis of national progress and prosperity.

IX.

FIXED AND FLOATING CAPITAL

The true foundation of all Science is a careful collection of facts, and a correct description of them. Nevertheless there is a class of writers who follow a different course, the result of which is apparently to bewilder themselves, and certainly to puzzle their readers. They embody crude notions in names and phrases, and thereafter those terms become to them the great facts of the case, the foundations of all their arguments and inferences, while the real facts are allowed to fall out of sight as if they were mere accidents of the question. The Terms become the rallying-cry of schools and sects, while the poor Facts are left to shift for themselves.

In all mental science, nine-tenths of the points of difference so keenly disputed arise purely from a confusion or unconscious disagreement in regard to the meaning of the terms employed by the belligerent writers. Metaphysical discussions have of late fallen somewhat into disrepute: and we do not regret it.

But the spirit which used to delight in the puzzles and colourless abstractions of metaphysics remains,—it is a part of human nature: and it has to a great extent compensated its exclusion from its old fields by invading others where it is still less wanted. Monetary science, indeed the whole field of political economy, has become overshadowed and darkened by this inburst of the metaphysical spirit. The present is a practical age,—practical science is recognised as the prime object of study: but this fact unfortunately has an unfavourable side, seeing that it has attracted from their congenial employment the metaphysical faculties of our educated classes, and transferred them into a field where their bewildering lucubrations do infinitely more harm than when merely beating the wind-bags of abstract speculation. The result is, that many more questions have now to be solved than before,—questions quite unknown to the practical mind of Adam Smith. Instead of having to deal only with the Facts,—and the facts in so wide a field as this furnish ample study of themselves,—we have to deal also with a whole host of bewildering Terms, which have become imported into the discussion.

We regret this: but we must meet the case as we find it. A writer who deals directly with the Facts can dispense with the term Capital altogether. It is simply a very vague name, a generic abstraction of doubtful meaning, for very plain things: and we should have preferred to write this work from beginning to end without using the word Capital at all. But had we done so, we should have failed to clear the science, as it

exists at present, of some of its most puzzling elements. We should have left the terms Capital, Fixed capital, Floating capital, Loanable capital, &c., floating in the air like wind-bags,—as weapons of controversy powerful because of their very vagueness and mystery. A "want of capital," a "scarcity of loanable capital," "a too great conversion of floating into fixed capital," &c., are phrases so frequently employed to explain monetary and commercial difficulties, that it is necessary clearly to understand what is or ought to be meant by those terms.

Capital is described as "Fixed," "Floating," or "Loanable," according to the conditions under which it exists. The terms employed to express those several conditions are exceedingly indefinite of themselves, and still more imperfect in the significations hitherto attached to them. As shown in a previous chapter, the conjoint agency of Financial companies and of Banking suffices to obliterate the distinctions between the various forms of property which are brought under its influence. By means of Finance, in fact, in co-operation with Banking, almost all kinds of property may be converted at will into "floating" capital. It is the special object and function of financial companies to mobilise "fixed" capital: or in other words, in exchange for an adequate security over fixed capital of any kind, to allow the persons who have so invested their wealth to reconvert the greater portion of it at will into a floating form, by giving them a draft, or power to draw upon a bank, for the amount. Every year this application of Finance is being more widely extended; and the time is not distant when

almost every kind of property existing in forms which we now call "fixed" will lose their character of immobilised wealth, and be rendered almost as convertible into money as commercial bills and Government securities are at present.

But in this chapter let us put out of view the operation of Financial or Credit companies of all kinds, and consider the transmutation of wealth into fixed or floating capital as if there were no other agencies than those of Banking and of Sale,—as if a man could convert his fixed capital into money only by selling it, or by getting it wholly or partially converted into money by the legitimate operations of Banking.

FLOATING CAPITAL.

"Floating" capital is a term equivalent in meaning to the secondary and narrower definition of Capital which we have given (on p. 86): namely, reserve-wealth in a mobilised form,—*i.e.*, in money, or in a form convertible into money at will on demand. "Fixed" capital is property in a form not readily convertible either into money or into other kinds of property. The difference between these two conditions of wealth is real and substantial: but the line of distinction between them cannot be sharply drawn. The various kinds of property, as regards "negotiability," merge into one another by almost imperceptible gradations. Moreover, the power of converting property into money depends not only on the nature of the property,

but also upon the state of what is called the Money Market.

If a man invests his reserve-wealth in building a factory or sinking a mine, that wealth unquestionably becomes fixed capital; if he keeps it in bank, it is unquestionably floating capital. Such is a broad or generic definition of these two kinds of wealth. But suppose a man buys £20,000 worth of shares or debentures in a railway or other joint-stock undertaking which yields a dividend: how stands the case then? These shares or bonds are from the first a marketable property. In ordinary circumstances, their possessor can sell them when he likes. Or suppose he invests a like sum in the Funds,—a species of property which is always negotiable or saleable, and at a steady value. In these two cases, and especially in the latter, it is doubtful if the capital so invested can be termed "fixed." In ordinary circumstances, certainly, it is not "fixed,"—the securities in which the capital has been invested being so readily convertible into money. Or, further, suppose a man deposits £20,000 with a finance or discount company, subject to a month's notice of withdrawal. Here it is a *bonâ fide* deposit of capital, repayable in money at a month's notice. Or, finally, suppose that the amount is deposited with a bank, subject to a week's notice of withdrawal. In all these cases there is a certain degree of fixture, *quoad* the investor, yet in the last case, at all events, it would be manifestly wrong to class the capital as "fixed."

The most perfect form of floating capital (now that private hoarding has been superseded by banking) is

unquestionably a deposit in bank payable in money on demand. This is the one extreme in the category of "floating" capital, as the building of a factory or such-like work, or the purchase of a large area of unreclaimed land, is the extreme of "fixed" capital. And in these cases the wide difference in the nature or character of the two forms of wealth—namely, Fixed and Floating Capital—is obvious.

FIXED CAPITAL.

Suppose a man invests £20,000 in building a factory and fitting it up with costly machinery: the portion of his wealth so invested is unquestionably, so far as he is concerned, "fixed"—it exists as a factory: and he cannot recover his wealth in the mobilised form of money, or in any other form, without selling the factory. Or suppose a company invests five millions in the construction of a railway: in this case also the capital is more or less "fixed," *quoad* the individuals who compose the company: it will not even bear interest to the company until the railway is constructed, and is working so as to yield a dividend. In each of those cases, the wealth has assumed a form which cannot be readily changed,—which cannot readily be reconverted into money or goods: it is not readily saleable or negotiable: it is Fixed capital.

Indeed, when a monetary crisis occurs, not only good railway shares and debentures, but even Consols and other kinds of Government securities, become fixed

capital: in other words, they become unnegotiable,—wealth from which their owner may derive interest, yearly or quarterly, but which for the time he is unable to convert into money. At such times, even wealth deposited in bank is liable to a similar unnegotiability, when represented by cheques, — even cheques, in a season of crisis, falling partially into disrepute. This is also, and to a greater degree, the case with good commercial bills: not necessarily from any loss of credit on the part of the issuers of the bills, but simply because the banks at such times (owing to causes which shall be considered afterwards) are unable to give money to the ordinary amount in exchange for or purchase of those bills.

The real nature of fixed capital — using the word capital in its wider sense, that of reserve-wealth in any form—may be further illustrated thus. A person builds or buys a ship: this is a conversion of capital into a fixed form. As long as the vessel remains in dock, it is fixed capital in an inactive form: it is not put to use, and it yields no return either to its owner or to any one else. If the owner use the ship himself, it becomes part of his stock in trade, part of the capital employed in his business,—just the same as a factory is to a manufacturer: he obtains a profit upon its use, but his power of reconverting it into money, or into other kinds of property, at his will is more or less uncertain.

Then, again, the factory may be leased, the railway may be subsidised, or the ship may be chartered and lent to others: in each of those cases the owner gets a return for his money sufficient not only as interest on

the capital which he has invested, but also to compensate for the loss of value which his property undergoes from tear and wear. His power of resuming possession of his capital in the form of money, or of exchanging it for goods of any kind, being lessened by the fact that he has allowed his property to pass at least for a time into the possession of others.

"Fixed" Capital, therefore, is wealth which is either temporarily removed from the free disposal of its owners, or which exists in a form not readily convertible by them into goods or money. *Quoad* its owners, the capital so invested is rightly termed fixed: but what becomes of the amount in the new hands into which it has passed in the process of creating this "fixed" capital,—for example, in the expenditure requisite for the construction of the factory, railway, or ship? And further, what relation has this fixture of capital by certain individuals to the amount of wealth available, either for loans, or for industrial employment by its owners, in the community at large?

If a man builds a factory, if a company constructs a railway, or a person builds or buys a ship, the capital so invested simply passes from one man, or set of men, into the hands of others. It is (or may be) fixed as regards the investors, but it passes to other men in the form of floating capital. It never becomes fixed *quoad* one man without simultaneously becoming floating capital in the hands of others. A conversion of floating capital into fixed, in a national point of view, involves simply a transfer of wealth: the result of which transfer is, that the capital sum no longer remains at the

free disposal of its owner, but either becomes reserve-wealth in bank belonging to others, or is added to the amount of money in active circulation. The capital so invested is "fixed" as regards its original owners, but it is not fixed in the hands of those to whom it is transferred. A company pays away several millions in the construction of a railway—it gets the railway in exchange for its capital,—but this capital is not destroyed by the operation: it continues in existence, and in full (or at least only momentarily impaired) efficiency, in the new hands into which it passes. A portion of it may pass into active circulation—in other words, may be kept in the pockets of individuals to meet their daily purchases—and thereby is withdrawn from the Money-Market; but by far the greater part of it is immediately re-deposited in bank, and continues to be loanable capital although its ownership is changed.

What some men pay away, others must receive. What, then, becomes of the capital in this secondary stage of the transaction: namely, in the hands of those to whom it is transferred?

It is a common thing for theorists on this subject to talk as if the capital invested in the construction of factories, railways, &c., became permanently fixed, and withdrawn from further use by the community. They speak as if the notes and coin employed in the construction of such works were actually converted into them,—as the stones withdrawn from a quarry are permanently locked up in the edifices for the construction of which they are employed. They speak as if the sovereigns and bank-notes were actually built up in factories and rail-

way-bridges,—permanently transmuted into embankments, engines, carriages, stokers, and railway porters. This, of course, is a total mistake. The capital invested in the construction of a railway is immediately transferred to the contractors, engineers, workmen, and others employed in making the line, in the form of payments and wages; and, either directly or indirectly, this money finds its way back to the banks in the shape of new deposits. The transaction involves merely a transference of banking-deposits from the shareholders of the company to the constructors of the railway. What is withdrawn by the former is returned by the latter. Or rather, hardly any capital is withdrawn from bank at all: it is simply transferred in bank from the credit of some individuals to that of others.

Let us take the case of the Railway, and see how far the construction of such a work involves a real fixture of capital,—or, speaking roundly, a withdrawal of capital in any shape from banks, which nowadays are the storehouses wherein is deposited nearly all the reserve-wealth of the community. On the part of the engineers, contractors, and other employés who belong to the middle class, the capital so received is redeposited in bank instantaneously,—or rather it is never withdrawn. These persons receive payment in the form of cheques, and those cheques are immediately paid-in—it may be to the same bank which issued them, or, at all events, to some bank with which the bank which issued the cheques settles accounts through the Clearing-House. In this case, obviously, no capital in any shape is withdrawn from bank at all: the banks have as much

capital in their keeping as before. On the other hand, that portion of the expended capital which is paid to the working-classes in wages is withdrawn from bank in the shape of notes and coin: but it quickly returns into bank again. In the course of a week or a fortnight, it is all paid to shopkeepers, who soon afterwards pay it into bank. Accordingly, in about a month's time, the entire amount of the floating capital withdrawn from banks for the construction of a railway, or suchlike work, is returned to the banks, reappearing in its old form. Therefore the only fixture of capital, *quoad* the community, which takes place in the construction of a railway, consists in the temporary absence from bank of that portion of the capital so invested which is paid in wages to the working-classes. And this absence is not, as we have seen, of any long duration.

But let us look more closely into this expenditure, in order to ascertain with precision how much of the capital becomes "fixed" even in the sense of being temporarily withdrawn from bank. In the first place it is to be observed that, although the construction of a railway or other large work may require an expenditure of five millions sterling, only a fraction of that amount is in use at one time. The amount is called up from the shareholders and invested in the work by instalments,—one instalment being nearly all spent before the other is used. Say that the work is to be completed in two years: the expenditure will amount to about £600,000 each quarter, or £200,000 a-month. But the capital withdrawn from bank is but a small part of this amount.

Nine-tenths of the expenditure is made by cheques, which at most occasion a transfer of securities at the Bank of England from one bank's credit to another's. In fact, it is only for the payment of wages of the labourers employed in connection with the railway, that capital in any form is withdrawn from [the banks at all. Now then, as only £200,000 of capital is called into play each month, and as only one-tenth of this expenditure is made in the form of money (notes and coin), and as this money finds its way back into bank in a month's time, the total "fixture" of capital occasioned by the construction of such a work would not at any one time exceed £20,000. And this amount, as we have said, returns to bank in a month's time at most.

This serves to explain how it happens that, although the so-called conversion of floating into fixed capital—in other words, the amount of enterprise in the construction of factories, railways, ships, &c.—is now so enormously greater than it was twenty years ago, the amount of floating capital not in bank (but "fixed" in the active circulation of the country) is comparatively little greater than before. The amount of money in England, in the form of bank-notes, is no greater than it was twenty years ago. The addition that has been made to the currency has been entirely in the form of coin (no notes under £5 being allowed in England), for the purpose of retail payments, such as shopping-purchases and wages. As appears from the returns of the Mint, this increase of the metallic currency, this absorption of capital in the form of specie, has averaged

about five millions sterling a-year.* And this amount represents, as regards the community as a whole, the sum-total of the results of our conversion of capital into a "fixed" form, as a necessary accompaniment of the vast increase of trade and industrial enterprise.

In point of fact, then, if we analyse the facts of the case, it appears that the only effect of the so-called conversion of floating into fixed capital, *as regards the community as a whole*, is represented by the additional amount of capital thereby absorbed in the form of money in the active circulation—*i. e.*, which is temporarily or permanently withdrawn from bank for that purpose.

In short, as regards an absorption of capital *quoad* the community as a whole, the so-called conversion of floating into fixed capital is equivalent simply to an increase of business or of monetary transactions. The capital which becomes fixed *quoad* one man becomes floating in the hands of others.† The greater the amount of buying and selling—at least in the shape of small or retail payments, such as wages and shopping-purchases—the greater the amount of money required to carry it on: hence an increase of trade and industrial employment (which is the natural accompaniment of an in-

* See *supra*, p. 43.

† Socially, indeed, the process, instead of being called a fixture of capital, might more truly be described as a liquefaction of capital,—it is a splitting up of a large amount of capital into a thousand small portions: and hence the construction of a railway, or other large work, is often and rightly proposed as a means of disseminating wealth in an impoverished district,—as, for example, in Ireland.

creased conversion of capital into a "fixed" form) produces an increased absorption of money, usually in the form of coin. At the same time it is to be borne in mind that this additional amount of capital absorbed in the circulation, does not cause any diminution in the amount of a nation's reserve-wealth, but is only a deduction from the addition which is yearly being made to that wealth. For, every increase of business, by increasing profits, *adds* to the capital or reserve-wealth of a country or of individuals, alike in a fixed and in a floating form. The five millions sterling which are being yearly absorbed in addition to our metallic currency do not constitute any deduction from the amount of capital in bank, available for loans; they are merely a deduction from the annual increase of that reserve-wealth.

Having thus winnowed the chaff and come to the net grains of truth in this matter, we find that the so-called conversion of capital into a fixed form is, *as regards the community as a whole*, identical, alike in its nature and its effects, with an increase of industrial employment, —occasioning a comparatively trifling addition to the amount of capital, "fixed" or absorbed in the circulation, in the form of money. It means simply a withdrawal of money from bank. And as no addition can at present be made to the issue of bank-notes, except an equal amount of gold be added to the stock in bank, this is equivalent to an additional requirement for specie.

A point of much practical importance remains to be noticed.—An increase in the monetary requirements

of the community may, and frequently does, take place without any increase of Trade or industrial employment. For example, at Quarter-day, when the dividends on the National Debt and other payments are made, nearly two millions sterling in notes and coin are temporarily needed from the Bank of England to make those payments, in excess of the ordinary monetary requirements of the community. The Bank pays out this sum,—and two or three weeks elapse before the money finds its way back to the Bank. This is actually as much a conversion of "floating" into "fixed" capital as the construction of a railway is. And in amount this absorption of money is far greater than is occasioned, during the same length of time, by the construction of any railway. This is not a point of merely theoretical importance. As a matter of fact, the Bank, in regard to the payments at Quarter-day, acts exactly as if these were, *quoad* it, a conversion of floating into fixed capital. (And so they are: only the Bank knows exactly the time when the money will return, and need not act with the same stringency as in other cases.) Hence it is that the month of October, when Quarter-day occurs contemporaneously with the increased monetary requirements of tourists and of harvest-time, is usually the most critical period of the year in monetary affairs. These periodical payments, then, have the same effect on the monetary condition of this country as any "fixture" of capital connected with the construction of a railway, or any other increase of industrial investments.

This fact serves to demonstrate the correctness of the conclusion at which we had already arrived—namely,

that the only effect of the so-called "conversion of floating into fixed capital," as regards the amount of wealth in a country available for employment, is represented by the additional amount of money required for active circulation—and which consequently is withdrawn from the banks for that purpose.

Hence, whatever be the effects upon the monetary or financial condition of this country attributed to the "conversion of floating into fixed capital," there always exists a practical and readily available test of the correctness of such opinions. All such conversions of capital from a "floating" into a "fixed" form, are exactly represented by the amount of money (notes and coin) withdrawn from bank, and temporarily or permanently * absorbed in the circulation,—*i. e.*, added to the amount already in use in the hands of the public. The only effect of such conversions, we repeat, as regards the community as a whole, is the amount of notes and coin withdrawn from the stock of money by which banks are enabled to carry on their business.

This brings us to the consideration of the last of the various terms applied, in monetary discussions, to the conditions of wealth—namely, to "loanable capital."

* The "permanent" absorption of money in this country—using the term in contradistinction to the "temporary" withdrawal of money from bank, which varies from month to month—is a quantity which can be definitely ascertained. All the specie absorbed in the circulation is represented in the returns of the Mint, while the amount of bank-notes absorbed by the public and by the non-issuing banks is represented by the returns of the banks of issue.

X.

LOANABLE CAPITAL

WHAT is meant in monetary discussions by "loanable capital?" Or rather, what is the legitimate definition of this term in Monetary Science?

Obviously, any form or kind of capital (reserve-wealth) may be loaned. A merchant or a producer may lend his goods on getting in exchange for them a bill, or promise to pay their value in money at a certain date: and the sum named in the bill includes the interest on the loan of the goods. One may also lend houses or land, getting interest on the loan in the form of Rent; or horses and carriages, books, plate, furniture, what you please,—getting interest thereon as Hire. But these various kinds of property are not "loanable capital" in the sense of the term as used in monetary science. When so used, the term has evidently a very much narrower signification. Well, then, what is the precise meaning in which the term can be legitimately employed?—what special form of Value is it which, in

monetary discussions, is designated, or which can be properly designated, as "loanable capital"?

As already shown, wherever the Banking-system is fully established, banks take the place of large capitalists. Banks are, in fact, the only source from which loans can be obtained. A capitalist keeps none of his reserve-wealth in his own hands, in his safe or his strong-box: it is deposited in bank: And when he draws it out, by making a loan, the bank's power of making loans is diminished just as if the loan were made by the bank itself. Hence "loanable capital," in discussions of this kind, means simply the power of banks to make loans,—or, to speak correctly, their power of allowing the public, in exchange for negotiable property deposited with them, to draw upon them for a given sum, whether by cheques, or in specie, or in notes convertible into coin of the realm on demand.

An embarrassment which takes the form of "a want of loanable capital" may have two different sources. It may be a commercial difficulty, or it may be a banking difficulty. In the one case the source of the embarrassment lies with the public; in the other case it lies with the banks. The embarrassment may arise from the public not having an adequate amount of property in a suitable form to offer to the banks in exchange for the power of drawing upon them: the public may not have the proper means for obtaining from the banks the required amount of money or banking-currency. Or it may arise from the banks not being in a position to make such exchanges of property or Value to the required extent: in other words, the banks may not be

able to undertake the liability of paying the amount of such exchanges in money. As long as the public, or the individuals who require this banking accommodation, have an adequate amount of suitable property to offer to the banks in exchange for the power of drawing upon them by cheques, or in notes or coin, the difficulty cannot possibly arise from "a want of capital" on the part of the public. In this case, the public is able to fulfil its part in the transaction: but the banks may not be able to meet the demand. Before they can safely give to the public a power to draw upon them, in exchange for property deposited with them, banks must consider whether they are in a position to meet the demand likely to be made upon them for payment of the liabilities which they thus incur in the form of money—notes or coin.

It is true that—as seen in our opening chapter—it is only a very small portion of the liabilities thus undertaken by banks that they are called upon to pay in money. Fully nine-tenths of the amount of these loans (so to call them) are never withdrawn from bank at all: the persons who get the loans, in exchange for the deposit of property, simply draw cheques for the amount, —which at most involves a transference of securities in the Bank of England from one bank's credit to another's—no money being withdrawn from any of the banks. But the extent to which banks are called upon to pay these liabilities in money is a variable quantity; and at certain times and under certain circumstances it becomes much greater than usual.

For example (1), during a commercial panic, payment

in cheques is sometimes refused, and payment in money required,—not from any distrust of the bank upon which the cheques are drawn, but because the creditor doubts whether his debtor has really an adequate balance at his banker's. In this way, at such times, there is an increased requirement upon the banks for payment of their liabilities in notes. Or again (2), the credit of certain banks may become impaired, and thereupon a portion of their customers demand payment of their deposits in coin, or in the notes of other banks whose credit is unimpaired. In the former case, the credit of the banks being unquestioned, they may meet the demand simply by issuing more notes, which the public are willing to receive. In the latter case, the particular banks which have become discredited must supply themselves either with more specie, or with an equal amount of notes from the other banks whose credit is untouched. Or lastly (3), a difficulty may arise without any loss of credit either upon the part of the banks or of the commercial classes,—simply owing to an unusual requirement for specie to send abroad: in this case the stock of specie in bank is unusually diminished, and the banks are forced to contract their usual amount of accommodation to the public, seeing that such liabilities may possibly have to be met by payment in specie.

Such, then, is "loanable capital;" and such are the various causes from which a want of loanable capital may arise. The source of the embarrassment may lie with the public, or it may pertain to the banks. In the one case the embarrassment is occasioned by the public not having an adequate amount of suitable securities to

offer to the banks; in the other, it arises from the banks not being in a position to supply the amount of accommodation requisite to meet the wants of the community.

Having reached this point, we are brought face to face with the most vital and practically important point in monetary science,—namely, the rate of interest—the charge made for the use of loanable capital. But before we can profitably discuss this question, we must first clearly elucidate the causes of banking-embarrassments, —in which are included the circumstances which at times tend to diminish the supply of loanable capital, and which thereby enhance the rate of interest.

XI.

BANKING EMBARRASSMENTS

In the opening chapter, we exhibited the wonderful system of Credit which an advanced civilisation has called into existence, and the immense benefits which that system confers upon the community. Let us now consider the embarrassments to which this exquisite monetary fabric is exposed, the manner in which they arise, and the remedies by which they may be met.

Banking embarrassments may arise from two different sources: namely, in connection either with the Note-issues, or with the Deposits. The common opinion which regards note-issues as the great source of peril to banks, is a mistake. The grand source of embarrassment to banks (and the sole embarrassment when banking is untrammelled by legislative restrictions upon the issue of notes) is a demand for specie; and in all circumstances, whether a bank's credit be perfect or unsound, such drains are made chiefly by the Depositors. Heavy drains of specie may take place upon a

bank—and such drains most frequently are made upon the Bank of England itself—without the slightest loss of confidence in the bank upon which the demand is made, and simply in consequence of an unusual amount of specie being required for export.

Whatsoever be the cause of the demand, there never is, or can be, a run for specie apart from a run for deposits. A run for specie in exchange for notes never occurs except in those rare cases where a bank loses credit, and becomes distrusted by the community. But even in those cases, the run for deposits constitutes by far the largest portion of a bank's embarrassments. And this is natural. Firstly, because under a free system of banking—*i.e.*, where there is no monopoly of the right to issue notes—the note-circulation of a bank forms a very small part of its liabilities. In Scotland, for example, the note-circulation amounts on the average to only one-fifteenth of the amount of each bank's deposits. Secondly, under any system of banking, if the holders of notes, who seldom have more than £5 or £10 in hand, lose faith in a bank, the depositors, who have thousands at stake, still more early and surely take alarm. The note-issues of a bank, however large they may be, are practically the least of its liabilities. There would be panics and runs upon the banks, and, practically speaking, to the same extent as now, though the banks did not issue a single note. In fact the most terrible panic and monetary crisis of recent times was that which occurred in 1857 in Hamburg, where the currency consisted entirely of specie.*

* See *The Economy of Capital*, p. 442-3.

It is also most worthy of notice, that a tremendous drain of specie may take place without the notes of the bank upon which the run is made experiencing the least discredit. Take two remarkable cases:—It was not a run for gold in exchange for notes which caused the memorable suspension of cash-payments in England in 1797: it was a demand for payment of deposits in specie,—the specie being required for export in payment of the loans which the British Government was then making to foreign Powers. Again, in the terrible panic of 1826, when the specie in the Bank of England was all but exhausted, the notes of the Bank not only circulated freely, and at their full value, but were even more eagerly in request than usual. All that the public wanted during those terrible crises was notes of the Bank; and as soon as the Directors reversed their policy of restriction, and issued their notes freely, panic was at an end.* In such cases, an increased issue of notes actually lessens the demand upon the bank for specie.

Moreover, under a system of "convertibility"—*i.e.*, where the banks are bound to pay coin for their notes on demand,—there cannot be any over-issue of banking-currency, or depreciation of the note. Why? Obviously thus. Bank-notes are issued either to depositors pure (*i.e.*, to persons who simply deposit their spare wealth with the bank), or to borrowers, understanding by that phrase persons who take negotiable securities to the banks to be exchanged for banking-currency. An actual depositor, being free to demand either notes or specie,

* See *The Economy of Capital*, p. 101-2.

will certainly not accept repayment in notes if he finds that the notes will not buy as much goods as the same sum in specie does. Neither will borrowers. A customer of the bank who discounts a bill, or who gets an advance upon securities, the amount of which is placed to his credit in the bank's ledger, can (like depositors pure) draw for the amount either in specie or in notes; and manifestly he will not take notes if their value or purchasing power is less than that of the specie into which they are convertible. Hence depreciated bank-notes, under a system of convertibility, cannot get into circulation at all; and if the notes be in circulation before the depreciation takes place, they will be quickly returned upon the bank which issues them.

Convertibility into coin, therefore, is a perfect safeguard against depreciation of note-issues. It is true that in countries of vast size, and where society is little centralised—as in India and the United States,—it is possible that notes may travel so far from the issuing bank that their convertibility is *de facto* impaired, and therefore ceases to be a perfect safeguard against over-issue or depreciation. Nevertheless, even in such cases, a remedy is not difficult to find: for example, by a process resembling that of the Suffolk Bank, adopted in the United States. Anyhow, this conceivable exception to the safeguard against depreciation which is afforded by convertibility of the notes into coin on demand, does not apply in any degree to England or France, where notes can be returned with perfect ease and promptitude to the bank which issues them.

A run for Deposits is the supreme embarrassment to

which Banking is liable. If such a run be persistent, no bank, however well-conducted, can withstand it; the bank must break, however solvent it may be: because the run is sudden and peremptory, whereas by far the greater part of the bank's assets do not consist of money, and cannot be converted into money in time to meet the emergency.

Such runs for deposits, happily, but seldom occur. If the direst, they are also the rarest, embarrassment which besets banking. A kindred difficulty more frequent, but far less serious, is that which arises from foreign drains of specie,—in other words, from an unusual demand for specie from the banks for the purpose of sending abroad. As such drains of specie figure prominently as the torments of every monetary system, they call for special notice.

AN EXTERNAL DRAIN.

"External" drains upon the banks of a country are always, and of necessity, made in the form of specie. Let us see how they arise, and what is their character.

The average value of the precious metals from year to year is nearly—for all practical purposes we may say perfectly—steady. Even the new supply from the marvellously-productive mines of California and Australia has not appreciably affected the value of the precious metals: the monetary wants of mankind—and especially Foreign Trade, in which specie is needed to pay the international balances—having expanded to an

equal degree. It is simply the temporary fluctuations of specie, the transient ebb and flow of the precious metals, which occasion the embarrassments so frequently experienced in this country. What, then, is the character of those drains of specie, and in what way ought they to affect the value of Money and the Rate of Interest?

(1) Those drains are local. There is never a dearth of specie all over the world. As specie becomes diminished in one country, it accumulates in another. As with the oscillations of the ocean, when there is low-water in one part of the world there is full-tide in another; so is it with the international movements of specie.

(2) Those drains of specie are very transient. They last only for a few months at most; after which time, the specie begins to flow back in the natural course of Trade. For example:—England suddenly imports a larger quantity of cotton than usual, or obtains a portion of her usual supply from some new quarter with which her commercial relations are imperfect: then she has to export a larger amount of specie than usual; but in a few months the cotton thus imported is exported in the shape of manufactured goods, and specie in still greater quantity comes back to this country. Drains of specie being thus local and transient, it is obvious that their effects might be wholly obviated by the establishment of an International System of banking—a subject fully discussed in the sequel of this work.

(3) Moreover, such drains of specie are really insig-

nificant in amount. No drain in our time has exceeded the amount of five millions sterling,* which is certainly less than five per cent of the amount of specie in the United Kingdom, and probably not three per cent of the amount of specie in France. Also it is only one-fourth of the amount of specie usually held by the banks of the United Kingdom (see *supra*, p. 6), and about one-third of that held by the Bank of France.

(4) As is obvious from the preceding statement, the portion of specie withdrawn by those drains is not really wanted at home. The metallic currency—the coinage in actual circulation—is never diminished; it remains as abundant as ever. The specie withdrawn for exportation is taken from the *reserve* of coin and bullion held by the banks, which reserve is kept for this very purpose. The amount is taken from a surplus portion of our stock of specie,—a surplus kept expressly for this purpose, and which would be altogether useless if not so employed.

(5) Moreover, it is to be observed that every such drain stops of itself. A drain of specie is not of indefinite quantity: it is simply an amount which we have to pay to some country in excess of the bills which we

* Mr Baxter, in his valuable little treatise on "the Panic of 1866" (p. 73-5), gives a tabular statement of what he calls the "drains of bullion" since 1823: but these are not drains in the common meaning of the term,—they include the entire variations between the successive maximum and minimum points in the amount of gold in the Bank of England, some of which extend over a period of more than two years. Moreover, they include "internal" drains as well as "external." The statement which we give above—namely, that no foreign drain of gold (using the words in their ordinary meaning) in our time has exceeded five millions—is correct.

hold upon that country. And every million of specie exported *pro tanto* lessens the drain. It is the very thing that is wanted to "correct the exchanges." And the specie thus exported returns to us, as it left us, in the ordinary course of trade. A drain of specie, instead of being like the escape of water from a reservoir through a hole that requires to be stopped, resembles an overflow into some reservoir of temporarily lower level; every such overflow naturally and inevitably tending to re-establish the equilibrium, and thereby to stop of itself. The specie does not leave us owing to any depreciation of our currency, and it will come back in the ordinary course of trade, without our taking any measures artificially to enhance the value of the currency in this country.

As in all the drains of specie which have occurred for the last forty years at least, the amount of gold exported was not actually wanted at home, and speedily returns, such occurrences do not, as a question of fact, invalidate the convertibility of the Note. On this point, the testimony of facts is indisputable. To take a recent example:—In the months of December 1863 and January 1864, the metallic reserve in the Bank of France averaged only seven millions sterling, while its note-issues, deposits, and other liabilities amounted to nearly fifty millions sterling: nevertheless the notes of the Bank, though not a legal tender, and liable to be cashed at any time, circulated as freely, and possessed the same value or purchasing power as before. Or take the extreme case of the Bank of England in 1826, when, owing to large foreign loans and madly speculative investments

abroad, the stock of specie fell to one million sterling. What occurred? Were the notes of the Bank in disrepute? Or were they depreciated to the slightest extent? Not at all. Although the wildest panic was then abroad, although every one distrusted his neighbour's credit, the notes of the Bank were even more eagerly sought after than usual. There was no cashing of notes at all: people were only anxious to get them. In fact the note-circulation of the Bank then rose to the extraordinary level of 25½ millions sterling. What is more, although a severe crisis was unavoidable, the aggravation of that crisis into a panic was occasioned by the Bank contracting its discounts and its note-issues; and the instant the Bank reversed that policy, and began to issue its notes again freely, the panic was at an end. Could there be a better or more striking proof of the fact that the temporary decline of a bank's stock of specie does not necessarily invalidate the credit of its notes? It is the dread of a bank's insolvency which alone causes its notes to fall into discredit: but a temporary decrease of specie in a bank of good credit produces no such effect. To the public at large, the notes of a sound bank are as good as coin,—or indeed better, seeing that they are more convenient for use.

The effect of an external drain of specie upon the credit of the note-circulation has been vastly overestimated. On such occasions, we repeat, there is no cashing of notes. The notes remain in as good repute as ever. The drain is made partly by depositors withdrawing their money in the form of gold; but chiefly — almost entirely — by persons taking bills to the

Bank, in order to be discounted, and thereupon demanding payment of the amount in gold. In 1797, and again in 1826, when the greatest drains of specie for export were made upon the Bank of England, and also in 1847, the note-holders never lost confidence in the slightest degree. In 1797, the notes actually continued in as good repute, and at the same value, after the suspension of payments in gold, as before. And in 1826 and 1847, the notes were entirely unaffected either in credit or value by the great export of gold. Such also was the case with the notes of the American banks during their suspension of specie payments in 1857. Not the slightest depreciation of those notes took place.* Therefore, when an external drain of gold occurs, there is no reason for diminishing note-issues, from any apprehension of the notes losing credit, and being brought to be cashed. Indeed in exceptional times (as during the war with Napoleon I.), when not only the bullion in bank, but even a considerable portion of our coins, or retail currency, were exported, an increased issue of bank-notes is imperatively called for. The public require such an increase of notes, to take the place of the exported coins—thereby maintaining the measure of value unchanged; and the note-circulation is as freely accepted at such times as if the vaults of the issuing banks were filled with the yellow metal.

Cause of External Drains.

Next, let us examine more closely the cause of those

* See *The Economy of Capital*, p. 294-6.

external drains of specie. They are by no means a proof of national indebtedness. For example, when our capitalists make a loan to some other country, a drain of specie from this country is frequently the immediate result of the operation. This occurred on a great scale on many occasions during the long war which this country waged with France, between 1792 and 1815. It has occurred on various occasions since then; and it is a natural, though not inevitable, result of all large loans which we make to other countries. It is obvious, therefore, that so far from being a proof of national indebtedness, an export of specie may be simply a result of other countries becoming in debt to us.

Moreover, apart from the operation of loans, a drain of specie may take place from this country although the balance of financial-transactions, as a whole, may be in our favour. An export of specie may be the result simply of a change in the currents of trade—of a transference of a portion of our trade from one quarter to another. For example, suppose that we could no longer get our usual supply of cotton from the United States, but were able to obtain it from Brazil: the first effect of this transference of trade would be an export of specie to the latter country. The United States import so largely from us, that our merchants (speaking generally) have always enough of bills on that country wherewith to discharge the payments for cotton. But Brazil takes comparatively little from us; so that, if we had suddenly to draw a large portion of our supply of raw cotton from that quarter, we should not be able to make our payments for cotton in the usual currency

of trade, namely bills, and consequently would have to export specie. If our exports to the United States remained undiminished, while our imports of cotton from them ceased, the result would be a flow of specie from North America to England, while a flow of specie took place from our shores to South America—supposing we drew our supply of cotton from that quarter. But our export of specie to Brazil might precede the receipt of specie from the United States,—thereby occasioning a "drain," or momentary diminution of our stock of specie.

Hence, although unquestionably an export of specie does in some cases indicate national indebtedness, in many others it bears quite an opposite character, and may be simply a result of other countries becoming indebted to us. In point of fact, as previously shown, this country does not suffer any diminution of its stock of specie. Its stock of the precious metals steadily increases, —the imports of gold and silver having exceeded the exports during the last six years to the amount of fully 30 millions sterling.* Accordingly, whatsoever banking-embarrassments may have occurred during that period—and some of those embarrassments, as in 1864 and 1866, have been of extraordinary severity,—they have certainly not been occasioned by any diminution of the stock of specie in this country. As regards the whole period, our stock of specie has been greatly increased; and in the two years when there really was a drain of specie—namely, in 1860 and 1861, when, owing to our unusually large imports of cotton from the United

* *Vide supra*, p. 67.

States, our exports of specie exceeded the imports to the amount of 4½ millions,—there was no crisis of any kind; whereas, in the subsequent years, 1862-66, when our stock of specie was increasing to an unprecedented degree (30 millions in the six years), our monetary difficulties have been incessant and almost unparalleled in severity.

How the Specie is Withdrawn.

Next, let us see by what mode specie is withdrawn from the banks, at times when an export of the precious metals takes place. The specie is not withdrawn (as once used to be supposed) by the cashing of notes, but by the discount of bills. When a merchant finds that he must export specie, in order to make a payment in some country upon which he cannot procure bills, he takes some of the bills in his portfolio (either Home bills, or bills drawn upon some other country than that where he has to make the payment) to his bank, and gets them discounted. The amount being then placed to his credit, he draws a cheque for the whole or a part of the sum, and requires payment in coin or bullion, which thereafter he sends abroad.

This is the process by which specie is withdrawn from the banks for export. There is no cashing of notes: the drain is made simply by some of the customers of the bank requiring payment of their deposits, or discounted bills, in specie.

Effect of Specie-Drains on the Banks.

Lastly, let us consider the effect upon the banks of those drains of specie for export. The withdrawal of specie, just described, does not involve any increase in the demand for banking-accommodation, but the accommodation has to be given in the form of all others most disadvantageous for a bank—namely, in specie. When foreign bills are procurable, the merchant who has to make a payment abroad discounts the requisite amount of bills in his possession, and with the proceeds in the form of notes or a cheque, he purchases the foreign bills which he requires. But when he cannot get foreign bills, then he withdraws the proceeds of the discounted bills from the bank in the form of specie. In the one case, he takes payment from the bank of the deposit which he has made (*i.e.*, the amount of the bills which the bank has discounted for him) in banking-currency—cheques or notes; in the other he claims payment in specie. In either case the amount of banking-accommodation is the same; but in the latter case the process is much more costly, or embarrassing, to the bank than in the former. The *financial* position of the bank is not affected. To make a deposit (by discounting a bill or otherwise) and then immediately withdraw it, manifestly leaves the debtor and creditor sides of the bank's ledger unaltered. But the form in which payment of deposits is required may make a vast difference in the position of a bank. Although no bank is able to pay all its deposits in specie, yet every bank is bound to do so if required.

Hence when a man makes a deposit with a bank by discounting a bill, and then withdraws the amount in specie, the transaction is highly unfavourable to the bank. The *monetary* position of the bank is *pro tanto* impaired. Although the bank's assets remain at the same ratio as before to its liabilities, the portion of its assets in the form of specie is diminished. Hence the bank's means of meeting its liabilities—its notes and its deposits being alike payable in specie on demand—are reduced.

This, then, is the difficulty which banks experience from a drain of specie. While receiving (by the discount of bills) assets not immediately realisable, they have to give in exchange an equal portion of their assets in the form of all others the most available and efficacious as currency. In fact, while giving out Value in the most negotiable of all forms (specie), and which is a valid tender under all circumstances, the banks (as usual) receive in exchange assets which are not suitable for general currency, and which are not immediately available to meet the demands for money which may be made upon the banks by their depositors. Accordingly, when an unusual requirement for specie occurs, banks have recourse to the most stringent measures to lessen the drain which is made upon them.

Defensive Measures of the Banks.

Let us consider the measures adopted by banks to meet this difficulty. In former times (for a century and a half after the establishment of the Bank of England)

the banks made no alteration in their charges at times when a drain of specie for export occurred: a rise of the bank-rate from 4 per cent to 5 per cent was the utmost that took place. But after the beginning of the great war with France in 1793, when our Government made large loans or subsidies to foreign Powers, and when heavy exports of specie ensued as a necessary consequence, the English banks met the diminution of their metallic reserves by contracting their business. They refused to give banking-accommodation to the public to the usual amount. This, of course, was a loss to the banks, inasmuch as they reduced their business, while lending at no higher rate than before. Hence such a course was never adopted by them except under circumstances which appeared to them to necessitate it. Moreover, as experience by-and-by proved, this contraction of banking-accommodation produced such serious disasters to the community as to create a panic, which reacted fatally upon the banks themselves. The numerous commercial failures which ensued in consequence of the merchants being refused the ordinary banking-accommodation, occasioned in turn heavy losses to the banks, and thereby shook the faith of the public in the banks themselves; so that a "run" for deposits arose—the most fatal embarrassment to which banks are liable. Undoubtedly, as banks are bound to pay all their liabilities in specie, a contraction of their liabilities, a refusal to discount bills to the ordinary amount, seems the most natural way of meeting a diminution of their stock of specie. But, on the other hand, it is found that the public disasters occasioned by such a course, give rise

to an embarrassment still more serious for the banks, by producing a Panic, and a general run upon the banks for payment of their deposits.

Within the last twenty or thirty years, another method of procedure has been adopted by the banks, to meet a drain of specie for export. They usually discount and make advances to the same extent as usual, but they greatly increase their charge upon those transactions. The bank-rate is raised from 4 and 5 to 8 and 10 per cent. This, of course, is most profitable to the banks. They greatly increase their profits while carrying on no larger business than before. And, on the whole, the community suffer less from this process than from the former one. It is better that the commercial classes should obtain their usual amount of banking-accommodation at a higher price, than not to get it at all. Nevertheless there are two great drawbacks upon this process. One of these is, that as this process is eminently profitable to the banks, the banks have recourse to it only too readily. The other is, that if carried beyond a certain point, the raising of the bank-rate becomes as mischievous in its effects as the old process of contracting the amount of banking-accommodation,—producing a Panic, which not only shakes the credit of the banks at home, and thereby causes an internal drain, but also brings our commercial bills into disrepute in foreign countries. In such cases the raising of the bank-rate actually intensifies the drain of specie.

This process of raising the bank-rate, as a remedy for a drain of specie, has been tried to the fullest extent of late years, especially since the crisis of 1857;

but the more it is tried, the more questionable does its efficacy appear. In the first place, it is obvious that if, when the bank-rate is raised in one country, as a means of checking the export of specie, a similar process be adopted in other countries, the effect must be *nil*. This is what has usually happened of late years. When the Bank of England raises its rate of discount to check a drain of specie, the banks of other countries do the same,—so that the flow of specie goes on as before: and the only result is, that Trade at home is checked, if not prostrated, by the raising of the bank-rate. True, when Trade is thus forced to collapse, less money than usual is needed, and money accordingly accumulates in the banks. But this is simply a war of the Banks against Trade and Industry.

Moreover, recent experience has shown that the potency of a rise of the bank-rate, even when made under the most favourable circumstances, as a means of influencing the ebb and flow of specie, has been greatly overrated. For many months last year the bank-rate in France was fully 3 per cent below the bank-rate in this country, and yet specie, instead of flowing from France to England, steadily flowed from this country to France. Nay, for several weeks last summer, the bank-rate in France was actually only $3\frac{1}{2}$ per cent, while in this country it was 10 per cent—there was a difference of $6\frac{1}{2}$ per cent!—and yet no specie was attracted hither from France at all.

In truth, the International Balance of trade and finance is the supreme power in determining the ebb and flow of the precious metals; and the rise or fall of the bank-

rate is comparatively powerless. If specie, from any cause, is due abroad—if the amount of payments which we have to make to a foreign country be in excess of the bills which we hold upon that country,—abroad the specie must go. You cannot stop it. When merchants must get specie to export, or else become bankrupt and ruined, not even a rate of 10 or 12 per cent will stop them from discounting their bills at the bank in order to get specie. The only persons who may be deterred by a high bank-rate are the voluntary exporters, — a class whose operations (as experience has amply shown) are at such times, if not mythical, at least utterly insignificant.

The Proper Remedy.

The proper course for banks which are largely connected with foreign trade, and therefore liable to drains of specie, is to keep a portion of their reserve in foreign Government securities,—by the sale of which they can provide themselves with specie when an unusual demand for specie is made upon them. All banks undertake to pay their depositors in specie when required; so that a supply of specie is indispensable to their business, — it is the basis of their highly profitable trade. When a cotton manufacturer gets an order for his wares, he willingly sends abroad for cotton. When a bank finds it necessary to get more gold in order to carry on its business, it ought to do likewise. Moreover, as we have before remarked, a drain of specie is not an illimitable quantity: its amount is fixed by

the operations of trade and finance; it tends to exhaust itself: but should it prove so large as to embarrass a bank, the right thing is for the bank to meet the demand by the cashing of foreign securities. If any loss arose from such transactions, the bank could easily repay itself without any appreciable inconvenience to its customers. If a bank, during a drain of specie, were to make an increased expenditure in order that it might safely maintain its business at the usual amount—if it were to purchase specie abroad in order to insure the convertibility of its notes as perfectly as before,—an almost imperceptible elevation of the rate of discount would suffice to reimburse this expenditure. For example: say that the usual loans and discounts of a bank are 20 millions; and that its stock of specie falls 2 millions below its usual amount, and that (by selling a portion of its foreign securities) the bank purchases specie so as to keep its metallic reserve at the usual amount. Two millions of its interest-bearing securities would thus be converted into specie, yielding of course no interest. But a rise of one-tenth in the bank-rate—say from $4\frac{1}{2}$ to 5 per cent—upon the 20 millions of its loans, would make the bank's business as profitable as before.

The raising of the rate of discount, doubtless, is a source of gain to the banks. But this gain is accompanied by two great drawbacks. (1) If the banks contract, or refuse adequately to expand, their accommodation to trade during a crisis, the bankruptcies may become so numerous as to endanger the position of the banks themselves. The distrust may increase into a panic, with its never-failing consequence, a run upon the

banks. (2) Although a high rate of discount immensely increases the profits of banks for a time, it is sure to be followed by a collapse of trade, and consequently by a diminution in the demand for discounts, which always partly, and in some cases wholly, nullifies the high profit made by banks during the crisis. Moreover, even though the crisis should not culminate in a panic, the high rate of discount occasions a serious depression of the markets; rendering the banks liable to greater losses than usual, owing to the failure of some of their customers whose bills they have discounted.

Hence it appears to be the true policy for banks to support Trade, and not at such times to make war upon it. Banks should aid commerce during a crisis to the best of their ability, and not seek an immediate profit by greatly raising the rate of discount, at the expense of a diminution of their own business after the crisis is past.

AN INTERNAL DRAIN.

An external or Foreign drain upon banks is always and necessarily made in the form of specie, coin or bullion. An internal or Domestic drain takes place either in the form of coin or bank-notes.

All the money (notes and coin) absorbed by an Internal drain remains in the country. But what becomes of it? Part of it, of course, goes into the hands of the public,—who either have need of it in order to meet a temporary increase in the requirement for payments in money, or who withdraw it for the sake of hoarding,

owing to a distrust of the banks. But a great part of it does not actually go out of bank at all. While one portion of the money absorbed by an internal drain goes into the keeping of the public, another portion is virtually "locked up" by the banks themselves. This latter portion is, indeed, withdrawn from the great fountains of currency—namely, the banks of issue; but it is locked up in other banks which have no power of issuing notes, or whose power of issue is limited to a fixed amount.

The cause of this lock-up or absorption of money in those banks is easily explained. When an increased demand for money on the part of the public arises, every bank has to prepare itself to meet this unusual demand. The London banks prepare themselves for the demand which may be made upon them simply by increasing their deposits in the Bank of England, —or, in other words, their power of drawing upon that establishment either by cheques or in notes and coin But the English provincial banks (which are not allowed to issue notes of their own, or not beyond a fixed amount) usually provide themselves with an extra supply of notes,—which they withdraw from the Bank of England, and take into their own keeping. The Scotch and Irish banks, on the other hand, being allowed to issue notes of their own upon condition of equally increasing their stock of gold, withdraw gold from the Bank of England to the required amount, and thereupon issue notes of their own to meet the increased demand for money on the part of their customers. A great portion of the addition which the banks thus

make to their ordinary reserves of money is never called for by the public. Nevertheless, this addition at such times has to be made; for no bank can be sure that an extra demand for money will not be made upon it. And thus an Internal drain affects the monetary condition of a country from two separate causes — namely, (1) from the extra amount of money actually required by the public, and (2) by the extra amount of money "locked up" in bank—that is to say, which banks must keep in hand to meet the demand, but which is not actually called for.

A serious domestic drain is occasioned or accompanied either by a Banking crisis or by a Commercial crisis, or by both. In fact, these calamities always, to some extent, occur simultaneously. They go hand in hand. The crisis may originate either in the one form or the other—either with Banking or with Trade,—and either Trade or Banking may be the greater sufferer: but the fortunes of both are more or less involved. A Commercial crisis menaces the credit of banks, by lessening, or partially destroying, the value of the commercial and other securities which form the chief portion of a bank's assets;—a Banking crisis brings fatal embarrassment upon the commercial classes, by the general contraction of banking-accommodation which at such times takes place, and also by a locking-up of the reserve-wealth of those classes in such of the banks as are forced to suspend payment. In either case an Internal drain, an increased demand or requirement for money, ensues.

A banking crisis is generally, if not always, a secondary symptom of financial embarrassment. It is bank-

ruptcies and losses in other quarters which occasion the distrust which eventuates in a run upon the banks. It is the failure of large mercantile houses, or of financial companies, which begins the mischief; and thereupon distrust attaches to the banks which are known to have been connected with the fallen establishments.

A Commercial Crisis.

A Commercial Crisis may originate from various causes; but whatsoever be its origin, its monetary features are in every case identical. At the outset it usually affects only some one great branch of trade. As failures multiply, the credit of the firms engaged in that trade is shaken: their bills (the wholesale currency of commerce) are regarded with distrust, and their creditors require payment in the more solid form of banking-currency—cheques and notes. Hence those merchants have to take a greater proportion than usual of their bills to the banks to be converted into banking-currency; and as even bank-cheques are in some cases refused when offered in payment by merchants connected with the embarrassed trade, a greater demand than usual arises for bank-notes.

Under the present monetary laws, the banks cannot respond to this exceptional and transitory increase in the requirement for notes, unless they to an equal extent increase their stock of specie,—which they never try to do, and which could hardly be done with sufficient promptitude to meet a sudden emergency; and accordingly they refuse to discount many of the bills

brought to them, and raise the rate of discount upon those which they accept. Instead of checking, this in many cases only increases the demand for discounts. As the rate of discount rises, the markets become depressed, and goods no longer bring their usual price. This, of course, tends to produce more commercial failures. Some merchants are ruined by having to force sales of their goods in a depressed market. Other merchants, again, who have a reserve of good bills, rather than force sales, take those bills to their bank to get a supply of currency, so as to enable them to wait till the markets return to their normal condition. They find it cheaper to pay 5 per cent more than usual for the discount of their bills than to lose 20 or 30 per cent by forcing a sale of their goods.

In this way a commercial crisis produces an increased demand for banking-accommodation from three separate but analogous causes. Firstly, as commercial currency at such times falls partially into disrepute—merchants being unwilling to take payment in bills to the same extent as usual from distrust of each other's solvency, —an increased supply of banking-currency (notes or cheques) is needed to take its place: so that more bills than usual are taken to the banks to be discounted—*i. e.*, converted into banking-currency. Secondly, the demand for banking-accommodation is further increased at such times owing to the fact that a high bank-rate produces a fall of prices, a depression of the markets: for, rather than make the usual sales of their goods in a stagnant market, some merchants take a greater amount of their bills than usual to the banks to be

discounted. Thirdly, as even cheques fall partially into disrepute at such times—not from distrust of the bank upon which they are drawn, but from a doubt as to whether the person who offers the cheque in payment really has a balance in bank to meet it,—a larger proportion than usual of the amount of the discounted bills is withdrawn from the banks in notes and coin.

As long as payment by cheques prevails to the ordinary extent, banks may meet an increased demand for discounts without any inconvenience to themselves, and consequently very profitably. But when, as above stated, a larger proportion than usual of the amount of the discounted bills is withdrawn in the form of notes and coin, the result is a serious embarrassment to banks. Nor is it one which they can wholly escape even by contracting their discount-business: for in such a case, their customers (either for the sake of meeting their engagements, or in order to profit by making purchases in the depressed markets) may make an increased demand upon the banks for payment of their deposits,—and at such times, as already said, the amount is withdrawn from the banks to a larger extent than usual in the form of notes and coin.

In this way, a commercial crisis occasions also a banking embarrassment,—which, of course, in turn reacts upon and increases the difficulties of the commercial classes. Let us, then, examine the normal features of a Banking Crisis.

A Banking Crisis.

This calamity occurs when some banks become discredited. Without credit, banking cannot exist. And when from any cause the public loses faith in a bank, and makes a heavy run for deposits, the establishment is almost sure to fail, even though it be really solvent,—that is to say, though its assets fully equal its liabilities. In truth, it is possible that an actually insolvent bank may weather the storm, when a solvent bank may be brought to the ground. A great deal depends upon the amount of its assets which a bank keeps in the form of currency. For example, suppose a bank which holds seven or eight millions sterling of deposits is run upon, and that it holds some three millions in cash or "at call," the ease and promptitude with which it would be able to meet the run would have so reassuring an influence on its customers that, almost to a certainty, the run would stop: and yet actually the bank might be insolvent after all. This, of course, is not a probable case —for an insolvent bank's reserve is usually very small compared to its liabilities: but we state it as showing how imperfect a test of a bank's solvency is its failure to meet a heavy run for deposits. On the other hand, a perfectly solvent, or indeed wealthy, bank may, and sometimes is, compelled to shut its doors in consequence of a panic. Although its assets be more than equal to its debts, it may be unable to convert its assets into notes or coin with sufficient promptitude to meet the demands of its panic-struck depositors.

This is the peculiar feature of a Banking-crisis,—it constitutes the grand element of difficulty in a run for deposits. It entails upon banks a necessity to provide a larger supply of notes and coin than usual; and this is a thing which they cannot readily do.

Remedies for an Internal Drain.

A potent means of lessening the dangers of a run for deposits is for banks to stipulate that no interest shall be paid except in cases where the depositors agree to give a week or a fortnight's notice before withdrawal; thereby giving the bank some time to convert its assets into money, in order to meet any unusual demand. This principle is adopted by nearly all the joint-stock banks of London. At the same time, it must be confessed that this system savours more of finance than of banking. And although there may rightly be diversities in banking, as in other trades, we cannot but approve, as more orthodox, the practice of the Scotch banks, the Bank of England, and some other banks, which have deliberately refused to put any restriction upon their depositors, and keep all the money intrusted to them at call.

Moreover, a mere delay of a few days, although of great use to a bank during a time of panic, is of no service if the panic does not in the interval subside. The grand difficulty is to convert into currency a portion of the bank's assets sufficiently large to meet the run. And the obstacle to this conversion is the ugly fact that there is only a very small amount of currency available

for such a purpose. It is needless to say that the coins and notes actually in circulation—*i.e.*, in the hands of the public—are not available. It is only the amount of specie in the banks—plus their power of increasing their note-circulation—which is available to meet a run for payment of deposits; and this amount is only about 20 millions, while the banking-deposits of the country amount to twenty times as much. Hence, under the present system, a very trifling increase in the monetary requirements of the community suffices to produce a most serious embarrassment.

During a panic, the demand made upon the banks is by no means exclusively, or even chiefly, for payment of deposits in specie. The banks which become discredited during a banking-crisis are comparatively few in number; and in making a run upon those banks, the public willingly take payment in the notes of other banks whose credit has not been blown upon. Indeed, in the case of the Western Bank of Scotland in 1857, it is a remarkable fact that its depositors willingly took payment even in the bank's own notes! And the result justified their confidence: for the other Scotch banks, knowing that the liabilities of the bank were amply covered by the wealth of its shareholders, agreed to cash the notes of the Western Bank even after it had closed its doors.

As the amount of currency in this country (permitted by the Bank Acts) is totally inadequate to meet a persistent run for payment of deposits, the first and most obvious remedy for the disasters of a panic is a system of Co-operation among the banks

themselves. In 1857, when, after the failure of the Western Bank, a run for specie began upon the other Scotch banks, these establishments, knowing each other's solvency, most wisely acted in concert,—each lending its stock of gold to its neighbours which had to sustain the run.* In this way a comparatively small amount of specie was rendered effective to meet the unusual pressure then made upon the banks. The great source of embarrassment to a bank, when a run is made upon it, is, we repeat, the difficulty—and, if the run be persistent, the impossibility—of converting its assets into money, whether notes or coin, with sufficient rapidity to meet the unusual demand upon it. A system of co-operation, in truth, is the only adequate means of sustaining solvent banks during such a trial. And although it is only natural that banks should see without regret the fall of rival establishments, a portion of whose business they hope to obtain, nevertheless this is a perilous game for them to play: for, in proportion as banks fall, the panic increases, and a run begins upon the other banks also. Hence a policy of selfishness and isolation is a dangerous game for banks to play: and we are not without hope that ere long the principle of Co-operation during a crisis will be freely adopted among the banks,—so as to insure for every solvent bank that aid from its neighbours without which no bank, howsoever well-conducted, can expect to withstand successfully a panic-run for deposits.

* For this fact, as well as remarks upon a System of Banking Co-operation, see *The Economy of Capital*, p. 114-118.

Three years have elapsed since, in my previous work on this subject, I advocated a system of Co-operation, or mutual support, as the most efficacious means of enabling banks to withstand the extraordinary demands to which they are liable during seasons of panic. The terrible Crisis of last year, when an organised conspiracy was directed against the credit of banks by a band of unscrupulous speculators, has amply demonstrated the advantage of the system which had been previously, and as usual ineffectively, recommended. It seems to be the lot of humanity never to learn save in the school of suffering. It is only the stern lessons of Experience that are effectual to produce important changes.

In Scotland and Ireland, a system of banking-co-operation can be readily established; but in England a serious obstacle is presented, owing to the vast number of separate banks in that country. Had the banking-system in England been allowed to develop itself under a regime of freedom, instead of there being about 300 separate banks, there would have been 20 or 30 large ones, with branches spread over the provinces. Owing to the consolidation of banks which of late years has begun, and which may be greatly facilitated by a wise revision of the Bank Acts, we hope to see the present obstacles to a system of banking co-operation in England greatly lessened, by many of the small banks voluntarily uniting themselves as branches to the larger establishments.

Nevertheless, a system of Co-operation, however valuable, is not enough. Throughout this chapter, we have

taken our Monetary System as it exists: and we have seen that a grand embarrassment to banks, during exceptional periods, arises from the inability to convert their assets into currency in order to meet the increased demand upon them. The Bank Acts greatly aggravate this difficulty: but how it is to be met is a question which must be reserved for consideration in a subsequent portion of this work.

XII.

THE RATE OF INTEREST

Among the tales of Oriental despotism, numerous as those of the Thousand and One Nights, there is one—there are many—of a good King who had a bad Vizier. The King had sincerely at heart the welfare of his people; but the Royal grace was narrowed in its flow by having to pass through the Vizier as an outlet. The covetous Prime-Minister levied from the recipients a tax upon the Royal favours. So he grew very rich; while the country suffered, and the people became very poor.

Among other measures of Royal care for the wants of the people, the King had constructed a vast Bund, or reservoir of water,—in order that, in seasons of drought, there might always be a supply of water for irrigating the fields, by the produce of which the people lived. In the East, nine-tenths of the population are dependent upon the soil for their subsistence; and the great desideratum at all times is, an adequate supply of water.

Give but water, and the produce of seed-time and harvest never fails. Water is the one thing needful. But the Vizier would have his profit on this also, regardless of the sufferings of the people confided to his care.

Now, a year of great drought came, and the people clamoured for water to irrigate their parched fields. It is not said whether the Royal reservoir was as large as the artificial lakes in Ceylon—the ruins of which, thirty miles in circumference, are still to be seen. But anyhow, the King had constructed it of such large size that it contained water enough and to spare for the whole surrounding country, even in seasons of the greatest drought. All that was needed was, that the sluices should be fully opened, and the precious streams would have fertilised the arid plains. But the Vizier resolved to make a large profit out of the wants of the people. So he opened the sluices only a little, pretending that he could do no more, and charged an exorbitant price for the supply of water. All classes suffered,—but not alike. The rich men of the country were able to get all they wanted, by paying the greedy Vizier the high terms which he exacted; and they reimbursed themselves for this by charging an exorbitant price for the grain and rice which they sold to the starving people. But the poorer classes, who had not money enough to pay so much, beheld their fields, the support of their homes, parched and barren: and a great famine overspread the land. In consequence, the people could not pay the usual taxes—which in the East are raised almost entirely in the form of a land-tax; and the King's tax-gatherers came back reporting that they could not get

the yearly tribute. Moreover, starving crowds began to gather about the gates of the Royal palace; and the King never went out without being besieged by crowds of his starving and angry people.

At last, when no taxes came in, and tumults began to arise, the King resolved to see for himself what was the matter. So he went forth, and found the fields lying brown and barren, and the rice-crops withered and yellow, and burnt up,—and the poor starving; while the rich repaid themselves for the Vizier's greed by throwing the burden upon the rest of the people: and the Vizier fleecing them all. And the King said, "Why is this? In the reservoir there is water enough and to spare. Why do you not get from it water for the fields, that so you may live and pay taxes?" And they said, "The Vizier will not give us the water unless we pay so much,—and we have given our all, yet cannot get enough of water." So the King was angry, and ordered the sluices to be opened to the full; and the fertilising streams ran in plenty over the plain,—and their running was like joyous music in the ears of the people: and the famine began to cease. And the Vizier was seized by the people, and thrown into the Bund, where he was drowned by the water of which he had been so avaricious. And the King's taxes were paid as before, and the angry discontent of the people passed away.

Now, what Water is to the population of Eastern countries, Money is to ours. In the East men live by the soil; in this country, our prosperity depends mainly upon Trade. And for carrying on that Trade, an adequate supply of money is indispensable. In the East,

payments in kind to a great degree still suffice for the settlement of accounts: the ryot, for example, who borrows a quantity of rice for seed or for food, repays in rice both the principal and the interest of the debt. But in England the system of barter is exploded, and every payment must be made, either directly or indirectly, in money. In this country, every payment must be made in money, or in forms of credit which are promises to pay in money. Therefore a wise Government should take care that no needless or artificial restrictions be placed upon the supply of this indispensable commodity.

Money (bank-notes or coin of the realm) is simply a form of wealth, into which all other kinds of wealth may be converted. And no artificial restrictions ought to be imposed upon such conversion. The State may, or may not, take into its own hands the supply of money for the community — it may issue notes, and import the requisite amount of specie to insure their convertibility, if it pleases; but if this supply be left to private parties, the State ought to take care, above all things, that there is not a monopoly,—and that, whatever regulations it may think fit to place upon the supply of banking-currency, all parties alike should be free to carry on that business. The State should either take the supply of money into its own hands,—or else it should leave the community at full liberty to supply its own wants, and to get those wants supplied in the manner which it finds most advantageous. A supply of money, we repeat, is as necessary to the prosperity of this and other countries of the West, as a supply of

water is to the lands of the East. And for a Government to make the supply of money a private and unchecked monopoly, is really as unwise and despotic a proceeding as it would be for an Eastern Sultan to confer a monopoly of the supply of water upon his Vizier or other favourite. Government may, if it please, require that every reservoir for the supply of the indispensable wants of the community be constructed upon certain principles, which have been found to be the most advantageous; but, subject to these conditions, the business of supply ought to be free to all parties alike. Whether it is better for a Government to take the supply of money into its own hands, or to leave that business to private establishments, is a debatable question; but there can be no question that for a Government to hand over the supply of currency as a *monopoly* to private parties, is a procedure of all others the most vicious in principle and the most mischievous in practice. It places the community, as regards the supply of money, as much at the mercy of these private monopolists, as the subjects of the Eastern King were at the mercy of the greedy Vizier for a supply of water.

A scarcity of money affects the Rate of Interest—the price of money on loan—just as a want of roads, or a deficiency of the means of transport, affects the price of goods to the purchaser. If all the corn in England were in store at York, and if there were no adequate means of conveying it to London, the price of corn in London would be commensurately enhanced. In the case of coal, this actually occurs whenever a hard frost lessens the means of transport, by sealing up the canals. In a

most striking manner, the same thing is exemplified in India. India at all times produces food enough for its entire population: and if the means of transport were as abundant there as here, there never would be a famine in India. Nevertheless tens of thousands frequently perish in India, in seasons of local drought, simply owing to the difficulties of transport, and the want of good country roads, by which food can be conveyed to the suffering locality. The price of rice, which, if it could be handed from the producer to the consumer, would be about a halfpenny a-pound, occasionally becomes twopence a-pound, owing to the want of the means of transferring it from the man who has it to the man who wants it.

In like manner does a deficiency of money raise the rate of interest. It destroys the negotiability of property; it obstructs the mobilisation of wealth; it prevents the conversion of goods into currency, which ought to be as free as the conversion of money into goods. The vast reserves of wealth become unavailable for use as loanable capital, because they cannot be converted into general currency. And hence the rate of interest is raised, not from any want of capital, or reserve-wealth, but because that wealth is no longer convertible into a loanable form. The effect is the same as if an immense reservoir of water were let out, for public use, only through a small aperture. Not the abundance of the water, but the size of the orifice, would regulate the price. However much water might be in the reservoir, the supply would be limited by the means of exit,—by the means of transferring the pre-

cious fluid to those who wanted it. The scarcity would be artificial: by simply enlarging the outlet, the supply would be ample. But as long as the restriction on the issue remains, the supply must be inadequate,—and a famine-price has to be paid for the contents of the reservoir, though the actual power of supply be really ample for the wants of the community.

The Rate of Interest—this is the most important practical point in the wide question of monetary science. The great Napoleon said that the only use of the Bank of France was to lend money at four per cent. And as a matter of fact, both in France and in England (prior to 1844), the rate of interest was generally—as Napoleon held it ought always to be—four per cent. For a century and a half the rate charged by the Bank of England, and all the other banks in this country, never varied more than one per cent—averaging about four and a half per cent. Whether or not this is a fair rate of banking profits—a fair charge for the conversion of good and readily convertible securities into banking-currency—we need not, from our point of view, stay to inquire. For we hold that the only legitimate test in such a case is, the law of Supply and Demand, operating under natural conditions,—that is to say, free from artificial restrictions of any kind.

We are opposed to fixing the rate of interest, or imposing a maximum upon that rate, by legal enactment. For two reasons: Firstly, because the cost of issuing banking-currency in exchange for securities (*i. e.*, the cost to banks of keeping specie sufficient to meet the demands which may be made upon them), fluctuates

from time to time; so also does the demand for such banking-accommodation on the part of the public: and either of those causes naturally calls for a variation of the rate of discount. Also, because the credit of borrowers, or the validity of the securities offered, varies, —so that in some cases a percentage (equivalent to a premium of insurance) has to be added to the ordinary rate of interest. Secondly, we are opposed to any legislative restriction upon the rate of interest, because it is an interference with the freedom of banking; and, in our opinion, the less legislation of a restrictive kind there is for banking, as for other trades, the better.

The rate of interest—by its effects upon the profits of industrial enterprise, and consequently, also, upon the employment of labour—is one of the most important elements which influence the wellbeing of a community. As nearly all our trade is carried on by means of credit, the Rate of Interest (one form of which is the rate of discount) forms a deduction from the profits of industry, and it may rise so high as to absorb all those profits. When the Rate is low or moderate, many industrial undertakings can be carried on, which must be abandoned when the Rate becomes high. Under a high rate of interest, the only kinds of trade which can be carried on are those which yield more than the ordinary rate of profits, or which are conducted by great capitalists, who can afford to stand a temporary loss. The trader of moderate means, or the rising man who seeks to compensate his lack of capital by industry and ability, has at such times to go to the wall; and has the mortification to see his business appropriated,

or his stock bought up, by some large capitalist, who can not only withstand the hard times, but make a profit by buying up the depreciated goods of his smaller neighbours or rivals in the trade.

As the rate of interest rises, one class of business after another becomes unprofitable. The national industry is contracted, labour is robbed of its wages, and thousands of the working-classes are thrown out of employment. Turgot, by a grand and striking figure, has likened the Rate of Interest to a flood-level "below which all labour, all cultivation, all industry, all commerce, cease. It is like a sea spread over a vast country: the summits of the mountains rising above the waters, and forming fertile and cultivated islands. But if that sea begin to ebb, in proportion as the level of the waters falls, the slopes of the mountains, then the plains and the valleys, come into view, and give birth to all kinds of produce. The rise or fall of the flood-level to the extent of a single foot suffices to inundate, or to give to cultivation, immense tracts of country." So is it with the Rate of Interest. Every rise to the extent of a single per cent above the ordinary level tends to suppress some branches of industry; and when the rate rises to 10 per cent, all trade becomes wofully contracted,—the field of labour is almost submerged, and scores of our merchants and thousands of our working-classes perish beneath the rising flood.

The Rate of Interest, speaking roundly, means the charge for loans of Money,—as the words Rent and Hire mean the charge for loans of most other kinds of Property. The rate of interest includes, as one of its forms,

the Rate of Discount,—*i.e.*, the charge which banks make for allowing their customers to draw upon them for Money in exchange for the deposit of suitable securities; in other words, in exchange for other kinds of property of a readily negotiable kind. And as banks are the great reservoirs of Money, and are the sole source from which a supply of general currency—whether coin, notes, or cheques—can be obtained, the Rate of Discount (or, as it is usually called, the Bank-rate) is the main element which regulates the rate of interest throughout the country. When the Bank-rate is high, private individuals demand a higher rate of interest for the use of their money than when the Bank-rate is low. Accordingly a railway company, for example, has to pay more for its loans (debentures) when the Bank-rate is high: and the same is the case in regard to all other transactions of a similar kind. As loans of money are frequently made for long periods, as in the case of mortgages, &c., the rate of interest charged for them does not invariably correspond with the rate of discount, *i.e.*, the Bank-rate of the day. Nevertheless the Rate of Discount is the main element or consideration which regulates the Rate of Interest throughout a country: and consequently it is a matter of the highest importance to ascertain the causes which occasion its fluctuations.

The special function of banks, and their sole function apart from the mere receiving of money in deposit, is to "mobilise" property—to give general currency, in the form of coin, notes, or cheques, in exchange for securities in the form of commercial currency (bills) or other

kinds of negotiable property. The cost of making those exchanges, plus a profit on the transaction, constitutes the Bank-rate or rate of Discount. This cost depends upon the various forms in which such exchanges are made. A Bank is liable to pay the amount of all such exchanges in coin of the realm: and the extent to which payment is called for in this form is the main element of the Bank's cost in the transaction:—

(1) If payment of those exchanges (discounts) were required only in the form of cheques, the cost to the banks of a country, as a whole, would be *nil:* for it would merely involve, by means of the Clearing-system, the transfer of so much credit (based upon securities) at the Bank of England from some of the banks to others. (2) If payment were required in notes, the cost of the transaction would be equivalent to the amount of specie (bearing no interest) which the banks would require to keep on hand to preserve the convertibility of the notes,—*i.e.*, to meet the demand which might be made upon banks to give coin in exchange for their notes: which usually is a mere trifle—the notes of a bank of good credit never being cashed by their holders except as a means of obtaining "small change." (3) But if payment of those exchanges is required from banks in the form of specie, the cost of the transaction becomes serious. And as all banks are liable to this demand for specie in exchange for the securities which they discount, they must keep on hand or in reserve an adequate stock of specie for this purpose,—the loss of interest upon which specie constituting a cost or outlay on their business, which cost (plus their profits) must be covered by the Bank-rate—

i.e., the charge which they make upon those who deal with them.

The mere amount of a bank's discount-operations, therefore, is but a minor point in determining the Rate of Discount: the great point is the extent to which the banks are called upon to pay the amount of their discounts in specie.

Let us consider, then, the circumstances under which the demand upon banks for specie-payments is increased,—or, in other words, the circumstances which naturally and properly occasion a rise of the Bank-rate. These may be classified under four heads: (1) an increase of trade and financial enterprise; (2) a commercial crisis, or partial break-down of mercantile credit; (3) a financial crisis, or collapse of speculative enterprise; (4) a Panic, or partial break-down of banking credit, producing a run upon the banks for payment of their deposits in notes and specie.

(1) An increase of trade and financial enterprise produces at most only a very trifling increase in the demand for notes and coin. It is superfluous to say that an increase of trade does not necessarily or usually occasion an increased demand upon the banks for specie for export. On the contrary (as notably in the case of France of late years*), a great increase of trade may be attended by a great influx of specie. But, to make the case perfectly clear, let us suppose that the expansion of business is purely of a domestic kind,—say, in the construction of railways, increase of manufactures, improving of land, &c. In such cases, the wealth employed

* *Vide supra*, p. 57.

is not sent abroad, and bank-notes and cheques alone are needed in its transference from hand to hand,—plus a small amount of coin required in payment of wages, especially if (as in England) there are no small notes. Now, as the additional amount of notes taken from the banks on such occasions are not meant to be cashed, but perfectly suffice of themselves for the requirements of the public, the only extra necessary cost to the banks during a time of increased trade is measured by the additional amount of specie in the form of coins which is then needed by the public. And this, accordingly, is the only necessary ground for a rise of the bank-rate on such occasions.

Nevertheless at such times there is an increased demand for banking-accommodation: every increase of business being attended by a larger creation of bills and acceptances, which in due course are taken to the banks to be discounted. Hence the banks find that they can increase the amount of their business; and every extension of a bank's discount-operations augments to an equal degree the bank's profits, even though the rate of interest remain the same. Accordingly, so far as profit is concerned, the banks may, with great advantage to themselves, enlarge the amount of their discounts without exacting a further profit by raising their charge thereon.* On the other hand, it is natural that banks, like other

* It must not be forgotten (although it often is) that such an increased demand for loanable capital is accompanied by an increased creation of capital, and especially of loanable capital, owing to the increase of trade and of profits. As trade augments, the profits of the nation increase likewise. In fact, it is the yearly increase of profits which mainly, if not alone, permits the yearly increase of trade.

traders, should seek to obtain the highest possible price for the commodity in which they deal. When the demand for banking-accommodation is increased, they may justly say—"It is true that an enlargement of discounts is very profitable to us, of itself; but if the demand for banking-accommodation is so urgent that we can exact higher terms for supplying it, by raising the rate of discount, and so obtain a double means of profit, we are entitled to do so."

(2) A partial collapse or break-down of commercial credit necessarily produces an increased demand for banking-currency, to take the place of the partially discredited commercial currency. Whatever be the primary cause of a commercial crisis, a fall of prices is its most serious concomitant. A sudden fall of prices in any branch of trade weakens the credit, it may be imperils the solvency, of the firms engaged in that trade. There are fewer buyers than before,—the whole operations of the trade thus temporarily embarrassed are contracted; and the holders of stocks, while reducing or wholly suspending their usual orders for goods, are placed in a serious dilemma. Their credit being diminished, those firms find that they cannot carry on their business by means of bills to the same extent as before. Payment by bills falls into disrepute, and payments in banking-currency are proportionately increased.

There are only two ways in which general currency can be obtained when an increased demand for it occurs. The merchants must either make sales of their goods to an unusual extent, or they must discount the reserve of bills which they usually keep on hand: sometimes they

have to do both. They are unwilling to take the former course—that is to say, to make forced sales,—because the market is already depressed, and extra sales would depress it still further. Rather than submit to this great loss, they take their reserve of bills to the banks to be exchanged for the currency which they require to carry on their business. This increased demand for discounts occasions only a small increase in the demand for notes, —by far the greater portion of the amount being used only in the form of cheques. And in so far as payment is taken from the banks in notes, these notes (as in case No. 1) are not meant to be cashed: they are needed simply to fill the vacuum created by the temporary disrepute of commercial currency (bills). Therefore, in ordinary circumstances, they may safely be issued without any increase in the stock of specie held by banks. Nevertheless, as the demand for banking-currency (notes and cheques) is increased, the banks are entitled to consult their own interests in meeting this demand. As we have already said, banks may make an increase of profits in such circumstances simply by enlarging their discounts, without raising the rate: but they will make a double profit if, while extending their business, they at the same time charge more for their accommodation. They may say, therefore, like other traders, "There is an unusual demand for our wares, and if we can turn the exigencies of the commercial classes to our own profit, we are justified in doing so."*

* It is a great mistake (frequently made) to suppose that an increased requirement for money is synonymous with an increased demand for capital in general. On the contrary, such an increase of

(3) A Financial crisis—in other words, a collapse of speculative enterprise carried on by joint-stock companies—produces generally the same effects as a commercial crisis. But it usually, as in 1825 and 1866, more immediately affects the credit of banks. The individual failures are more serious in their magnitude than commercial failures, and they also produce a more widespread trepidation on the part of the general public. Financial companies have usually a large subscribed capital, and frequently also they hold a considerable amount of capital deposited with them by the general public. Hence the collapse of such companies produces a wider alarm than is occasioned by purely commercial failures. And this widespread feeling of alarm almost invariably leads to a "run" upon the banks which are known or believed to have been connected with the fallen companies. As the securities of those companies become worthless, the banks which are known to hold those securities lose their

monetary requirements may, and usually does, coexist with a decrease in the demand for capital in general. This is notably the case during every commercial panic. Whenever, from any cause, any large failures or suspensions take place, the demand for capital as a whole diminishes,—but the demand for money augments. Every failure or suspension necessarily diminishes the amount of business, and consequently the demand for the use of capital on loan. The suspended firms, of course, entirely cease business; and the panic or distrust occasioned by the suspension of those firms induces other firms to contract their operations. Hence the demand for capital as a whole is lessened. But the monetary requirements of the commercial classes increase. An increased supply of bank-notes is required, although the ordinary amount of business is diminished. The effect, then, is simply the same as if an increased demand arose for some particular commodity—say cotton or iron,—for one kind of capital, while the general demand for capital is greatly lessened.

credit, and are immediately subjected to a severe run upon their deposits—for payment in money of the wealth which the public had intrusted to their keeping.

(4) A Banking-crisis, or a run for deposits, is different in its effects from any of the previously mentioned causes which affect the rate of discount. What is the natural or legitimate effect of such a crisis upon the Bank-rate? Obviously, a raising of the Bank-rate can have no effect whatever in checking a run for deposits. It cannot place any deterrent charge upon the public who make the "run," for the depositors are entitled to claim their money, without charge, on demand. Moreover, a rise of the Bank-rate at such times, by increasing the failures, and extending the embarrassment to the general trade of the country, tends only to augment the panic, and consequently the run upon the banks. True, banks which are "run" upon have of course less money to lend: all that they have, or can procure, is needed to meet the demand for repayment of their deposits. But in their case it is useless to raise the charge for discounts, for actually they have no money to lend at all: they must stop discounting. At the same time, there are always some banks whose credit remains unimpaired, and who consequently are not "run" upon. Those banks are able to continue their ordinary business of discounts and advances: and as, at such times, owing to the embarrassment of the other banks, their discount-business is largely increased—as the customers of the embarrassed banks, which are no longer able to make the usual advances, have to come to them for accommodation,—these fortunate banks (so

to call them) are entitled to profit by their advantage, by raising their charge—*i.e.*, the bank-rate. This rise of the bank-rate, as we have said, only increases the panic, and still further weakens the position of the other banks. Nevertheless—as a bank, like any other trader, has only to look after its own interests—it is quite justifiable for any bank to take this course, provided that its superior strength and credit are due only to itself. But if this bank, say the Bank of England, has acquired its superior position in consequence of long-established legislative privileges, and to the greater power conferred upon it of meeting the demands of the public by an issue of notes, it is a very doubtful question how far such a bank is justified in using its privileges as a means of increasing its profits, by a process (the raising of the bank-rate) which directly tends to augment the losses of the commercial classes, to extend the panic, and thereby to further weaken the position of its rivals, the other and non-privileged banks.

Banks, doubtless, are entitled to charge on their operations the highest rate of profit which they can get. But then, there must be free competition, as in other trades. Any farmer who thinks it advantageous to offer his grain in the market at 65s. the quarter, while his neighbour stands out for 70s., is at liberty to do so. In like manner, any banks which are willing to enlarge their accommodation to the public upon moderate terms—either contenting themselves with a lesser amount of profits than if they were to raise their rate of discount, or feeling assured that such a course will be more profitable to them in the end, by increasing their amount

of business—ought to have the power to do so. But in order that the rate of discount may be regulated by the normal law of supply and demand, it is obvious that there must be no monopoly of the right to issue banking-currency in the form of notes. All banks alike, subject to the same conditions, ought in this respect to have the same powers.

One more point remains to be noticed. Even when all banks alike are equal in the eye of the law—that is to say, if they all had the same rights subject to the same conditions,—the rate of discount may be abnormally affected by the nature of the legislative restrictions imposed upon the issue of bank-notes. The bank-rate, as we have said, under natural circumstances, is determined by the cost which banks incur in meeting the liabilities which they take upon themselves by the discount of bills,—which cost is represented by the amount of specie which they have to keep in hand to meet the demands which may be made upon them for payments in specie. If legislation imposes any other condition upon the issue of bank-notes, the rate of discount is thereby artificially heightened. And hence, in the interests of Industry, which is the basis of national prosperity, care should be taken that no other restrictions are placed upon the issue of bank-notes than such as are indispensable to render the notes a safe and acceptable currency for the community.

A single illustration will suffice to show the artificial difficulties which may be placed upon the supply of currency by monetary legislation. No one doubts that if our Government wanted a loan of ten or twenty

millions sterling, the Chancellor of the Exchequer could get it readily and upon easy terms. It would be subscribed in the City in the course of a few hours. But if it were required that the loan should be paid on a certain day, at Somerset House, in the form of money, whether gold or bank-notes, the loan could not be got. There is reserve-wealth enough in the country; but how is it to be loaned?—how is it to be advanced in the form of money to the Government? Ten or twenty millions in gold or notes, in excess of the ordinary amount of currency, would be needed on a single day, between the hours of 10 and 4, for the one purpose of withdrawing deposits from the banks and paying the subscriptions to the loan. And as none of the metropolitan banks, except the Bank of England, are allowed to issue notes,—and as the other English banks are prohibited from extending their issues even for a single day or hour, however great may be the demand for their notes on the part of the public,—it is obvious that the ten or twenty millions in notes or gold, needed for the exceptional and momentary purpose of subscribing to the loan, would require to be furnished by the Bank of England. But the Bank, under the present system, could not do this, or anything like it.

All that would be wanted, in such a case, is a momentary supply of bank-notes. But most of the large banks at present are not allowed to issue notes of their own at all; and such of the provincial banks as are allowed to issue notes are prohibited from doing so beyond a certain amount, however willing the public may be to take the notes of those banks. Hence, in

this supposed case of the Government loan, however abundant the amount of wealth ready to be loaned, the Government could not get the loan taken up,—simply from a want of the medium by which the required amount of wealth must be transferred. Capitalists may be ready to lend,—the Government is ready to receive; yet the loan could not be made. The extra amount of bank-notes, in this case, would be needed only for a few hours: by 5 P.M. they might all be returned to the Bank of England, and cancelled. This would be the natural way of settling such a transaction,—and it is the way in which such transactions used to be settled. But, under the monetary laws passed in 1844-5, such an increased issue of banking-currency, however momentary, is impossible.

Under our present Bank Acts, the restriction upon the issue of bank-notes is certainly greater than is requisite; and, consequently, ever and anon the rate of discount is raised above the level which the natural circumstances of the case warrant. In fact, the issue of banking-notes is at present so fettered that occasionally the supply becomes quite inadequate to the requirements of the public; and, in consequence, not only is the bank-rate raised to an exorbitant point, with a proportionate loss to the public and a general collapse of trade, but, in times of crisis, the banks themselves become incapable of meeting the demands upon them,—so that the Bank Acts have to be suspended.

XIII.

OUR MONETARY SYSTEM

THE sounder and more elastic a country's monetary system is, the more prosperous will that country be in times of peace, and the more powerful in war. War, as a grand exception, tests a monetary system to its base. It is only a thoroughly wise and scientific system that can prove equal to a country's requirements in such an emergency. Happily, England has not been involved in any great war for the last fifty years; and for the last eleven years we have enjoyed the blessings of uninterrupted peace. Nevertheless, during those eleven years our country has suffered from monetary crises to a most unwonted extent. Why is this? The banking-classes, and all the upholders of the present Bank Acts, have been profuse in explanations. At one time, they say, the embarrassment was produced by bad harvests; at another, by "over-trading;" at another, by "new companies;" at another, by our "cotton-trade;" at another, by "a too great conversion of floating into fixed capi-

tal;" at another, by the "destruction of capital in the United States;" at another, simply by the increase of trade and employment in this country. Those explanations are for the most part exceedingly hazy and unsatisfactory; but even if they were substantially correct, they are so numerous and so diverse as to suggest, of themselves, that our monetary system cannot be well framed, since it is liable to serious embarrassment from such an endless diversity of causes.

Let us, then, examine our Monetary System, as established by the Bank Acts of 1844-5, and its practical working.

The Act of 1844 enacted that no new banks of issue should be established in any part of the kingdom. And the then-existing English banks of issue (the Bank of England excepted) were prohibited from increasing their note-circulation beyond the average amount of those issues at the time when the Act was introduced. The banks of Scotland and Ireland were allowed to issue notes beyond that amount, on condition that for such extra issues these banks should keep on hand an equal amount of gold. Such issues accordingly yield no profit. Moreover, no provision was made for the lapse of issues arising from any of those banks discontinuing business: so that any vacuum in the Scotch or Irish currency arising from this cause can only be filled up by the other banks of those countries increasing their stock of gold in order to extend their note-issues. The provincial banks of England (*i.e.*, all the English banks of issue except the Bank of England) were placed on a somewhat different footing. They were not allowed to extend their "fixed issues"

(*i.e.*, the average amount of their note-circulation in the spring of 1844) upon any terms,—not even on the condition of holding gold to an equal amount. If any addition to the English note-circulation became necessary, it was to be supplied by an increased issue on the part of the Bank of England. It was also enacted that, in the event of any of the English banks of issue discontinuing business, the vacuum thereby occasioned in the currency should be supplied by the Bank of England only to the extent of two-thirds of the lapsed issues. And this only on two conditions: namely, that the Bank of England should be empowered to do so by an Order in Council; and also, that the profit upon these additional issues of the Bank (for which it was not required to keep an equal amount of gold) should go to the State. With this exception, the Bank was not allowed to extend its note-issues unless it equally increased the amount of gold locked up in its Issue Department.

The effect of these regulations has been greatly to reduce the number of the banks of issue in the kingdom, and to some extent to reduce the amount of note-currency. When the Act of 1844 was passed, the number of banks of issue in England (exclusive of the Bank of England) was 275,—it is now 187; in 1844 the authorised issue of those banks was £8,648,853,—it is now £6,771,256. Thus, since 1844, the banks of issue in England have been reduced in number by 88, or nearly one-third; and their authorised circulation has been diminished to the extent of more than one-fifth.*

* The "fixed issues" of the English banks (exclusive of the Bank of England) now stand as follows:—

In lieu of the £1,877,597 of lapsed English issues, the Bank of England has been authorised to issue notes of its own to the extent of £1,000,000,—leaving a deficiency to the amount of nearly a million (£877,597). And as a lapse of the authorised note-issues of Scotland has taken place to the extent of £337,938, the total diminution of the note-currency from this cause at present amounts to rather more than £1,200,000.*

Thus the actual and natural result of the Bank Acts has been greatly to reduce the power of issuing bank-notes in this country below what it was twenty-three years ago. But, ignoring this not unimportant decrease, let us say simply that under the Bank Acts the power of issuing bank-notes has been fixed at its amount in 1844. What are the consequences? Since that time the foreign trade of the country has trebled in amount, and the home trade has likewise greatly increased. At the same time our note-currency has not been allowed to expand at all. The effects of an expanding trade combined with a fixed note-circulation are twofold,—the one permanent, the other temporary; and both of them are injurious to the community.

In every progressive country like ours, the amount of money required to store up the increasing wealth of the community steadily increases; while more money also

131 Private banks, with a maximum issue of .	£4,032,616
56 Joint-stock banks ,, ,, ,, .	2,738,640
Total, ...	£6,771,256

But, as these banks have at all times to keep carefully within this maximum, the actual power of issue is less than £6,000,000.

* For a detailed account of the provisions and working of the Bank Acts, see the chapter on the Bank of England in my previous work on *The Economy of Capital.*

is required in active circulation, to carry on the operations of trade and industry. Almost all large payments in this country are made, not in money, but by cheques; but all retail payments, and the weekly wages of operatives, are made in money, either coin or notes. Now, as the note-currency is at present fixed in amount, the steady increase which takes place in the amount of those retail payments can only be made by means of a corresponding addition to our stock of the precious metals in the shape of coin. It appears from the returns of the Mint and of the Bank of England, that no less than 120 millions of gold have been added to the coinage since the passing of the Bank Acts; and as long as those Acts continue in existence, an additional amount of gold must annually be imported in order to meet our increasing requirements for currency. Moreover, besides this necessary and progressive increase in the active circulation of the country, an additional and steadily increasing amount of money is required in the banks, to represent the reserve-wealth of the country. The wealth of the nation increases every year to the extent of at least 150 millions sterling; and the portion of this wealth which is deposited in bank is likewise increasing. For example, during the last ten years, the deposits in the London joint-stock banks have doubled in amount; and, in consequence, the amount of money which those banks keep in reserve has increased in an almost equal proportion. A corresponding though doubtless lesser increase has taken place in all the banks of the country.

Thus we see that more money is needed now than in

1844 for two reasons:—(1) In the active circulation, to carry on the increased and yearly increasing operations of trade and industry; and (2) in the stock of money held by banks to represent the increased and yearly increasing amount of their deposits. More money must be kept in hand by the banks, while more money is needed by the public in permanent circulation. As the further issue of bank-notes is prohibited, one of two things must happen. Either money, the measure of value, must become scarce and rise in value; or else the currency must be largely added to in the costly form of specie. As we have seen, the coinage has been immensely increased since 1844; and we may be thankful for the discovery of the new gold-mines, because but for them no such addition to our currency could have been made, and a disastrous scarcity of money would ere this have befallen the country as a necessary result of the Bank Acts. During the last quarter of a century—*i.e.*, since the passing of the Bank Acts,—the development of the cheque-system has produced a vast economy of the currency; and but for this, even the doubling of our gold-currency which has taken place would not have sufficed to meet the wants of our ever-expanding trade. But as the cheque-system has now become universal, we cannot expect much new saving from this source. Hence the yearly additions to our gold coinage will probably become larger than ever. At the same time the produce of the gold-mines is declining. In such circumstances it is easy to foresee that, if the Bank Acts continue in operation, the country will ere long be landed in a serious dilemma.

So much for the permanent and constant effects of the Bank Acts. As England is extremely rich, doubtless she has hardly felt the loss of the five millions a-year, which has been sunk in additions to her metallic currency. It is as regards the future that those permanent effects of the Bank Acts are chiefly to be deprecated. But there are other effects of the Bank Acts, not permanent in their operation, but of frequent occurrence, and of far more serious importance, from which the country has already suffered most disastrously.

The enactments of the Bank Acts may be classed under two heads: the one Negative and the other Positive. These Acts not only prohibit any extension of the note-circulation, but they enjoin that the power of issuing notes shall be diminished whenever a diminution takes place in the stock of specie held in bank. Such a diminution takes place whenever more gold than usual has to be exported; and also whenever the import of gold into this country does not take place to the usual amount. Both of those occurrences are merely temporary in their duration: in a few months at most the operations of trade restore the equilibrium, and bring our stock of specie up to its normal level. But in the interval, brief as it is, the provisions of the Bank Acts inflict grievous disaster upon the country. When the stock of gold in the Bank of England is at its ordinary amount (about 14½ millions), the export of two or three millions of gold suffices to produce a dearth of money and a serious commercial crisis. The Bank's power of issuing notes being diminished to an equal amount, its means of carrying on its business (*i.e.*, of giving banking-

currency in exchange for commercial currency and other kinds of negotiable property) are reduced below the ordinary amount. The public do not ask for its gold,—all that they want is its notes to the usual amount; but this the Bank is prohibited from issuing. A dearth of money takes place, and the Bank-rate of discount is raised to an exorbitant point. The direct effect of this is, that the commercial classes and others have to pay a double price for their discounts, and for advances upon securities, by means of which all our trade is carried on. But this is the least part of the evil. In consequence of the dearth of money, the purchasing power of the community is lessened, and in many branches of the wholesale trade, the usual sales of goods can only be effected at 20 or 30 per cent below the ordinary price. As a necessary consequence, bankruptcies multiply, commercial credit is shaken, scores of merchants and manufacturers are ruined, trade is contracted, and tens of thousands of the working-classes are thrown out of employment.

Moreover, a diminution of the stock of gold in the banks often takes place without any export of specie at all. Gold may flow towards our shores to the usual amount—the stock of specie in the country may remain undiminished,—nay, it may even increase; and yet a decrease may take place in the amount of gold in the banks, with the same disastrous results as we have above described. In England no notes are allowed to be issued of less value than £5,—and £5-notes are useless in making many of the smaller kinds of payments, and especially in the payment of weekly wages. Hence

whenever trade becomes brisk, and more employment is given to the working-classes, an extra amount of sovereigns is withdrawn from the banks, and ultimately from the Bank of England. In consequence, under the Act of 1844, the Bank's power of issuing notes is contracted; and thereupon the rate of discount is raised, checking trade and diminishing employment, in order that there may be less need for money, and that the sovereigns which have been withdrawn may be brought back into the Bank.

There is yet another point which calls for special notice. There are tides in the currency,—steadily recurrent periods at which the currency must rise above its normal level, in order to respond to a temporary increase in the monetary requirements of the community. There are monthly tides, quarterly tides, and a great autumnal tide. (1) The first of those tides occurs on the 4th of every month,—the day on which the great majority of our home-trade bills fall due. It is the settlement-day between the great wholesale houses and the retail-dealers who purchase their goods. As nearly the whole of those monthly payments are made by cheques, hardly any money is needed,—no money is withdrawn from the banks; the amount is only transferred from one man's banking-account to another's, or at most from one bank to another: so that the effect produced upon the money-market by those monthly payments is very slight. (2) The Quarterly tides are produced by the Government payment of salaries, of the dividends on the National Debt, &c., and also by the payments of rent and other quarterly obligations on the part of

the community at large. These quarterly payments occasion a very considerable increase of the active currency, —an extra million and a-half of money being at such times withdrawn from the Bank of England, and put into temporary circulation. A considerable portion of the Government-payments of salaries, and also of the quarterly dividends, are made to clerks and other persons of small means, who do not keep a banking-account, and who therefore cash the cheques which they receive, spend a portion of the amount, and keep the remainder beside them. Moreover, whether or not the recipients of those quarterly payments keep banking-accounts, all of them have considerable payments to make of debts incurred during the quarter: so that large sums in money are at such times paid to tradesmen and others, and thus temporarily absorbed in the circulation. But in three weeks at most, all this money finds its way back into bank, being re-deposited after a little delay, and sometimes after passing through several hands. (3) The Autumnal tide is occasioned chiefly by the operations of the agricultural classes, and to a lesser extent by tourists and holiday-seekers. The operations of harvest, and the large sales made at the great autumnal fairs, are carried on almost entirely by means of money, and not by cheques. Tourists also who go abroad, and the whole body of holiday-seekers who in autumn proceed to the moors or the sea-side, provide themselves with an extra supply of money. In these various ways a considerable amount of money (about 2 millions) is temporarily withdrawn from the banks. The currency at such times must expand; and the only way in which the requisite

addition can be made to it is by withdrawing an equal amount of money from the banks.

This statement does not exhaust all the causes which periodically affect the currency; but these three—the monthly, the quarterly, and the autumnal—are those which are the most distinct in their character, and the most invariable in their recurrence. The monthly tide is a small affair,—but every three months it is coincident with the quarterly tide; and the two when thus occurring together exercise a notable influence on the money-market. But the great monetary climacteric of the year—the annual crisis in the mercantile world—is produced when the monthly and quarterly tides are coincident with the great autumnal tide. At these times the currency rises much above its ordinary amount. A spring-tide is produced, as when the sun and moon are in conjunction, and raise by their attraction the waters of the ocean high above their usual level. This critical period of the monetary year takes place at the beginning of October. In the first week of that month the monetary requirements of the Government and the public suddenly increase to the extent of about 2 millions; but within three weeks afterwards all this money is returned into the Bank again. This demand for additional currency is purely temporary,—it arises from causes perfectly well understood, and periodic in their occurrence,—its duration also can be safely predicted. Nevertheless, the Bank of England raises the rate of discount quite irrespective of those considerations. It ignores all the facts of the case, save the single one that more currency is momentarily required; and on this

sole and transient ground the Bank-rate is frequently raised to an exorbitant point at such times, thereby ever and anon producing serious losses and embarrassment to the community at large.

It is obvious that if any export of gold, or any increase in our home-trade (requiring more currency in payment of wages), occurs contemporaneously with those periodic monetary tides, a most serious crisis is produced. Under the present system, it does not matter whether the increased demand for money be for export, or simply for internal circulation; neither does it matter whether this withdrawal of currency from the Bank be for an indefinite time or merely for a few weeks. In all cases alike, the Bank raises the rate of discount, frequently to an exorbitant degree. For example, let us see what took place in the autumn of 1864, when a crisis of considerable gravity took place.

In October and November 1864, there was no drain of gold for export at all: on the contrary, the imports of gold during these two months exceeded the exports to the extent of 2½ millions, of which amount nearly 2 millions (£1,800,000) were added to the stock of gold in the Bank of England. Nevertheless, in the ten days ending on 7th October, the Bank-rate was raised from 4 per cent to 7,—an increase of 75 per cent in the rate of discount throughout the country. Why was this? Let us show the facts briefly in detail.

In the first place, there was the usual monetary tide which occurs in the first week of October, owing to the quarterly payment of the dividends, &c. This periodic increase in the monetary requirements of the Govern-

ment and of the public, as already stated, amounts to about two millions—of which about £500,000 is needed in sovereigns, as the Bank is not allowed to issue notes of less value than £5. The notes and the sovereigns thus temporarily required for the quarterly payments were all (as usual) returned into the Bank during the three or four weeks following: they were all back by the 8th of November. So much as regards the effects of the periodic monetary tide.

But, concurrently with this periodic tide, our Home-trade was on the increase: more employment was being given to the working-classes, and more retail-money was needed in payment of wages. Let us see what effect this had upon the Bank. In addition to the £500,000 in coin usually required at this autumnal quarter-day, and which speedily returns into the Bank, fully £1,800,000 in sovereigns was drawn out of the Bank in the seven weeks ending on the 1st of November; and of the total amount of sovereigns (£2,382,776) withdrawn from the Bank between the 13th of September and the 1st of November, £1,600,000 were still out of Bank in the second week of December. Where were they? What had become of them? In the first place, as the returns of the Irish banks show, nearly half a million of sovereigns (£496,342) had gone to Ireland. Several causes, of which the Dublin Exhibition was the chief, produced a greater requirement for currency in the shape of bank-notes in Ireland; and, under the Bank Acts, the Irish banks are not allowed to issue notes beyond a fixed amount (*i.e.*, the amount of their note-circulation in 1844), unless they cor-

respondingly increase their stock of gold. Hence, more of their notes being needed by the public, the Irish banks had to provide themselves with more gold by withdrawing half a million of sovereigns from the Bank of England. Nearly an equal amount of gold (£417,089) simultaneously went to the Scotch banks. Trade in Scotland was brisk: moreover, the second week of November witnesses one of the great half-yearly monetary tides in Scotland, corresponding to quarter-day in England. From those causes the Scotch banks had temporarily to issue more notes than usual; and (like the Irish banks) they are prohibited from doing this save on the condition of equally increasing their stock of gold. Neither in Ireland nor in Scotland was there any increased demand for gold. Of the million of sovereigns taken by the Scotch and Irish banks, not a single coin was actually needed by them. The Bank Acts of 1844-5 compelled these banks to lock up this amount of gold idly in their vaults: that was all. But for those Acts, not a single sovereign would have been withdrawn by these banks from the Bank of England. The drain was wholly occasioned by the provisions of the Bank Acts. And in this way £914,000 of the sovereigns withdrawn from the Bank of England is accounted for. What became of the remainder—of the other 900,000 sovereigns withdrawn from the Bank? It was absorbed in the circulation of England. Trade and employment were expanding, and more retail-money (small change, in fact) was needed in payment of wages, &c. In Scotland and Ireland, £1-notes suffice for all the wants of trade, in payment of wages, &c.; but in England, where no notes are

allowed to be issued of less value than £5, these retail payments must be made in coin.

Here, then, there is a twofold inconvenience in our present monetary system. In the first place, whenever more notes are needed in Scotland and Ireland, the banks of those countries must withdraw an equal amount of gold from the Bank of England, although not a single sovereign of this amount is actually needed by them. In the second place, whenever an increase of employment, and consequently of wages, takes place in England, more sovereigns must be withdrawn from the Bank, in consequence of there being no £1-notes, which would serve the purpose equally well.

Yet this is but a small part of the dilemma. During the time when this extra amount of sovereigns was withdrawn from the Bank, in October and November 1864, foreign gold was flowing into the Bank in large quantities: so that, in point of fact, during the twelve weeks ending on the 6th of December, upwards of £300,000 more gold was taken into the Bank of England than was during the same period withdrawn from it by the internal drain. Why, then, the great rise in the Bank-rate from 4 per cent to 7?

Any one who studies the statistics of the Bank of England and the action of the Directors must be struck by two remarkable facts: namely, that however momentary the withdrawal of gold from the Bank—as at quarter-day,—or however slight the diminution of the Bank's stock of gold, a most disproportionate and exorbitant rise takes place in the Bank-rate. Take, for example, the condition of the Bank (as

shown by its weekly returns) during the semi-crises of 1864 and 1865. The following table shows the average amount of the Bank's stock of gold, of its reserve of notes, and of its discounts and advances, for each period during which the Bank-rate continued unchanged; and also the amount of foreign gold which during each of those periods was flowing into the country:—

Period.	Coin and Bullion.	Reserve of Notes.	Discounts and Advances.	Rate of Discount.	Balance of Imports and Exports of Gold, marked *plus* and *minus*.
1864.					£
June 15 to July 27	13,700,000	6,700,000	20,760,000	6	June + 698,598; July — 474,641
July 27 to Aug. 3	12,930,000	5,100,000	20,470,000	7	Aug. + 557,763
Aug. 3 to Sept. 7	12,820,000	5,030,000	20,480,000	8	Sept. + 545,475; Oct. + 1,120,140
Sept. 7 to Nov. 22	13,050,000	6,250,000	20,250,000	9	Nov. + 380,947
					Excess of Imports + 3,302,943
1865.					
Aug. 2 to Sept. 27	14,210,000	6,230,000	21,530,000	4	2 months + 645,000
Sept. 27 to Oct. 7	13,000,000	4,360,000	24,170,000	4½ 5 6	10 days + 100,000?
Oct. 7 to Nov 9	13,320,000	5,570,000	20,570,000	7	9 weeks + 2,500,000
					Excess of Imports + 3,245,000

The facts exhibited in this table suggest many important deductions, but we shall restrict our criticism only to the leading points. The first of these is, the smallness of the variations in the Bank's stock of specie compared with the greatness of the changes in the Bank-rate. In 1864 a diminution of only £650,000 in the Bank's stock of specie was held sufficient to

justify an elevation of the rate of discount from 6 to 9 per cent. In 1865, a diminution of barely £900,000 in its stock of specie was attended by an elevation of the Bank-rate from 4 to 7 per cent. This is certainly a startling fact. Moreover, in neither case was this great rise in the Bank-rate occasioned by an increased competition for banking-accommodation. As shown in the table, the average amount of the Bank's discounts and advances was actually less than usual at the times when the Bank was charging the highest rate for its money. It thus appears that those striking elevations of the rate of discount were not due in the slightest degree to any increased demand for banking-accommodation. In truth, they can only be explaind by the fact that the Directors make a most trifling decrease in the stock of specie a ground for largely increasing the gains of the Bank's shareholders.

There is yet another important point in this table to be noted. During those semi-crises, there was no foreign drain of specie at all. On the contrary, on both occasions gold was flowing into the country to a greater extent than usual. In the months of 1864 during which the Bank-rate was raised from 6 to 9 per cent, the imports of gold (as shown above) exceeded the exports by $3\frac{1}{2}$ millions sterling. In the months of 1865 during which the Bank-rate was raised from 4 to 7 per cent, the imports of gold exceeded the exports by $3\frac{1}{4}$ millions sterling. Under the Acts of 1844-5, it is gold alone that is taken into account; but to prevent any doubt as to the perfect fairness of the preceding statement, let us add that the imports of silver during the critical months

of 1864 exceeded the exports by about half-a-million sterling; and during the critical months of 1865, they fell short of the exports by barely £100,000.

How are those facts, so anomalous of themselves, and so disastrous to the trade and industry of the country, to be explained? Partly by a peculiar provision of the Act of 1844; and partly by the monopoly conferred by that Act upon the Bank, which allows the Directors to make exorbitant charges simply with a view to increase their gains. The peculiar provision of the Act to which we refer is that which enjoined that for all notes issued beyond the limit of 14 (now 15) millions, the Bank must keep in the Issue Department an equal amount of gold. This gold is never needed by the Bank in connection with its note-issues: a few thousand pounds in coin is all that is ever required for the cashing of the Bank's notes,—such cashing taking place only as a means of procuring "small change," in consequence of no £1-notes being allowed. Hence nearly seven millions of the Bank's stock of gold are immobilised: this large amount of specie is locked up in the Issue Department, where it is never needed. In this way it happens that, if there are fourteen millions of gold in the Bank, little more than one-half that amount is actually available. This is a great waste: it virtually nullifies almost one-half of the average amount of gold held by the Bank. When there are 14 millions of gold in the Bank, the Directors act as if there were little more than seven. Nevertheless, even making allowance for this absurd provision of the Bank Act, there is no adequate reason for the great elevations

of the rate of discount which the Directors make contemporaneously with such slight fluctuations in the Bank's stock of gold as those above referred to. These elevations of the Bank-rate are in great part due simply to the fact that the Bank possesses a monopoly of the currency, and can act as it pleases, unchecked by the wholesome influence of competition.

Such is the practical effect of the Bank Acts in ordinary times: we shall endeavour to show how they operate during a severe monetary crisis.

XIV.

THE PANIC OF 1866

ANY person who was in the City during the critical days in May 1866, will never forget the scene of excitement and trepidation which was then witnessed; and those who were not eyewitnesses had the spectacle fully described to them in the newspapers of the day. What is important to our present inquiry is to point out the essential features of that great Crisis.

Three important points have to be noted at the outset. Firstly, the catastrophe neither originated in, nor produced, any mistrust in the note-circulation of the country. Neither the notes of the Bank of England, nor those of the 200 other banks of issue in the kingdom, were at any time distrusted. Secondly, the catastrophe was not connected in any way with a drain of gold from the banks, either for export, or even for internal use. And, lastly, it was not in any respect a commercial crisis. Commercial failures and suspensions followed, as in such cases they must do: but they were

simply a consequence, and in no way a cause, of the catastrophe. The trade of the country was not only perfectly sound, but (what is remarkable on such occasions) its soundness was universally admitted after the crisis had occurred.

The peculiar feature of the catastrophe was that it was essentially a banking crisis. It originated with the lenders, not with the borrowers of money: not with Trade, but with the establishments which lend to Trade. The cause of the panic was a distrust of the banks and other establishments which receive in deposit the reserve-wealth of the public. The grand and sole feature of the crisis was a run for deposits. The public—from causes of which we shall afterwards speak—lost faith in the establishments in whose hands they had deposited their reserve-wealth, and they made a sudden run upon those establishments in order to get back their wealth, in the form of money, into their own keeping.

A panic is never wholly unfounded. It vastly exaggerates the grounds of alarm, but it does not originate them. Let us see, then, what were the facts and causes which, gradually and almost imperceptibly accumulating, led up to the sudden outburst of Panic, which broke like a thunder-clap over the City in the second week of May.

Although the panic was unexpected, to a degree never paralleled before, a preparatory disquiet had long been prevalent in the City. Although that disquiet did not become discernible by the public till March, it had existed in the City for seven months previous to the culminating panic. It began in the first

week of October 1865, when the Bank of England suddenly raised the rate of discount from $4\frac{1}{2}$ to 7 per cent. That was the minimum rate for first-class short-dated bills, and advances on other securities were then charged still higher: in fact, on the 9th October, many first-class bills could hardly be discounted even at 10 per cent. On that day the disquiet almost amounted to panic: and if any great failures had then taken place, the panic of the subsequent year might have been forestalled. The monetary facts in connection with this semi-crisis have already been stated and commented on in the preceding chapter, and we need not recur to them.

Two months later, in December, a slight and transient drain of gold for export occurred; and as the year 1866 began, the Bank of England raised its minimum rate of discount to 8 per cent. Nevertheless, although a *sourde* disquiet prevailed in the City, things went on pretty smoothly till the month of March, when the Joint-Stock Discount Company collapsed. This was the initial event in the history of the recent panic: and as such, it is worthy of notice.

The Joint-Stock Discount Company was a grossly mismanaged concern. In the hope of rivalling the large dividends paid by many of the banks and financial establishments, this Company, instead of contenting itself with the safe business of discounting commercial bills, dealt largely in advances to contractors and other kinds of risky—but, if successful, highly profitable—business. The business was badly managed: some of the advances proved thoroughly bad investments; and at the same time so much money was

locked up in long loans that the Company became embarrassed. The Directors explained the state of affairs to the shareholders, and proposed a call of £5 per share. Upon hearing this bad news, the shareholders, with more rashness than judgment, took the direction of affairs into their own hands. They appointed a new set of Directors, who, after inspecting the accounts, reported that a call of £2, 10s. would be sufficient to make all right. But soon they found that the old Directors were in the right, and that if the larger call were not made, the Company could not go on: and they resigned. Thereupon the shareholders, naturally enough, broke forth in a chorus of anathemas against the old Directors, as if they were a pack of swindlers, although most of those men were the largest losers by the failure; and, in the end, this sadly mismanaged Company went into Chancery.

Owing to the stormy meetings which accompanied the collapse of this Company, and the violent language applied by some of the speakers to the Directors of the Company (duly reported in the newspapers), the affair made a great impression in the City; and Discount and Financial companies became objects of distrust and suspicion. And, in many cases, deservedly. But there are at all times parties who are ready to foster such suspicions, with a view to their own profit. These are the speculators on the Stock Exchange,—men who make a profit by buying shares at one price and selling them at another. They do not need to hold any shares themselves at the time when they sell them,—for they are not bound to deliver the shares until a fortnight after

they have sold them, by which time (if their "bearing" operations are successful) they can easily get shares at a lower price than that at which they sold. Thus these speculators have a very wide scope for their operations. The process is this:—Suppose a combination of those speculators resolve to operate against a company whose shares are quoted at £20. Some of them go on 'Change, and offer a large amount of shares at that price. This tends to depress the value of the shares in question. Next day, others of the confederates offer shares of the same company at £18; on the third day at £16; by-and-by at £14, and so on. In this way the men who sold the shares (not one of which they held) at say £20 or £16, before the time for delivering those shares to the purchaser, can provide themselves with the shares at £16 or £12,—thereby making a handsome profit.

Such is the object of those "bearing" operations which were carried on so largely during April and May 1866, with such disastrous effects to the general public. The first effect of such operations is, that the *bonâ fide* shareholders, the persons who really have shares to sell, take alarm, and sell their property at the depreciated value,—thereby increasing the fall in the market-price of such stock. Secondly, as the public see the shares of the company falling so fast and so seriously, they begin to think that there is something rotten in the business: and those who, as depositors, have intrusted their money to this company's keeping, hasten to its office to withdraw their money. In this way, that most fatal of all forms of panic—a run for deposits—begins: and as the "bearing" operations continue, the run waxes

greater, till the establishment has to succumb, and closes its doors. As a final calamity, the company gets into Chancery: the heavy costs of liquidation, and the great losses sustained by a forced realisation of the assets, quickly shift the balance to the wrong side of the ledger; and the shareholders, instead of having, it may be, a sound-going business, are glad to escape with the loss of all their paid-up capital.

Those "bearing" operations are legal, if not legitimate, in themselves; but unquestionably, during the panic of 1866, they were conducted in a most shameful manner,—by the propagation of lying reports, and the adoption of the most unscrupulous means of shaking the credit of perfectly solvent establishments. In fact, this "bearing" conspiracy is the most infamous which the Stock Exchange of this country has ever witnessed, and it produced disasters which have brought misery and ruin into thousands of honest homes.*

* Although the panic of 1866, with its organised "bearing" operations, is in its leading features a novelty in this country, it had an almost exact parallel in the United States in 1857. The initial event in the terrible American crisis of that year was the downfall of the Ohio Life and Trust Company (an establishment which held upwards of a million sterling of deposits, and which made advances upon financial securities), just as the late panic was initiated by the collapse of the Joint-Stock Discount Company. Thereupon, as in our own case, an organised system of "bearing" operations commenced; and one monetary establishment after another was attacked, till the distrust swelled into panic. The *Times* correctly said—"There is actually a powerful combination for the avowed purpose of bringing all the principal undertakings to ruin. A large body of active persons are known to be associated for the purpose: they influence the press to work out their views, and are alleged not merely to operate with a joint capital, but to hold regular meetings, and permanently retain legal advisers, whose chief vocation, it may be assumed, is to discover points that may enable the validity of each kind of security to be called in question,

The collapse of the Joint-Stock Discount Company, which led to the subsequent distrust of so many of the London monetary establishments, was occasioned by its so-called "financiering" operations; and it was the suspicion, more or less well founded, that other monetary establishments had embarked in similar operations, that helped to augment the distrust. Financial business is *per se* a perfectly legitimate kind of enterprise. It is a business which has attained a great development within the last few years, and it supplies a real want. It provides money at a high rate of interest for companies and undertakings which, owing to the nature of the securities which they have to offer, cannot obtain advances from banks or from pure discount-companies.

and thus to create universal distrust." (*Times*' City Article, Sept. 10, 1857. See also the City Article for Sept. 15 and 17, and the New York correspondence in the *Times* of Sept. 14 and 24, 1857).

A run for deposits in specie thereupon commenced on all the banks of New York; and what did those establishments do? They knew each other's position,—they knew that they were all perfectly solvent: but they knew also that it was impossible to meet the run for deposits made upon them; and by common arrangement they all suspended specie-payments simultaneously. The effect was the same as that which attended the vastly more serious suspension of cash-payments in this country in 1797: the panic at once subsided. Neither did the slightest depreciation of the notes of the New York banks ensue. During the few weeks that the suspension lasted, the notes circulated freely at par: indeed, by a curious accident, they even rose to a premium compared with gold. "According to advices received to-day," said the *Times* of October 31, "good sight-bills could still be purchased at an exchange of 101. The extraordinary fact is therefore exhibited of the inconvertible currency of the New York suspended banks being actually at a high premium compared with the specie-currencies of other countries. That is to say, a bill on London could be purchased in the notes of the New York suspended banks at a price which, after allowing for interest and all charges, would bring back in gold a larger sum than had been paid for it!"

What is wanted in such cases is the loan of large sums, not repayable till (speaking roundly) one or two years. The financial companies supplied this want: and as long as they are judiciously conducted, they are of immense advantage to the country, and may reap large gains for themselves. Some of those financial companies, however, had not conducted their operations judiciously: still more—and this was the great cause of the catastrophe of 1866, in so far as it had a reasonable basis,—some banks and discount-houses had likewise engaged in this "financiering" business, which to such establishments is more or less inappropriate. It was essentially a Financial, and not a Commercial crisis.

There are three different kinds of monetary business carried on in the City; and it was the attempt to combine them which, under the pressure of the panic, served to undermine the position of our monetary establishments. Those different kinds of business, it is true, are not actually incompatible,—they *may* be all carried on together: but they are quite different in their methods of procedure, and each requires a different kind of ability on the part of the managers.

First, there is Banking. A bank receives the reserve-wealth of the public, and lends it out. As its deposits are liable to be called up at any time, it is the duty of a bank to lend only on good commercial bills, or other securities which are readily convertible into money; and it ought also to keep an ample reserve of money immediately available to meet the demands of its depositors. Risky loans, or loans not repayable for a long period, are incompatible with safe banking. *Secondly*, there is

the Discount-business. A discount-business, pure and simple, is the simplest and safest of all kinds of monetary trade. If a discount-house (as used to be the rule) deals only with its own money, it does not need to keep any reserve, nor can its failure ever make a "crash." It can never suspend payment, for it has no payments to make: it has no liabilities to the public. If some of the bills which it has discounted prove bad, it has less money to lend out again: that is all. For example, suppose a discount-house has £900,000 of paid-up capital, and deals only (we shall say) with three months' bills: then it advances £300,000 on bills the first month; £300,000 the second month; and a like sum in the third month. If some of the bills which it discounted in the first month prove bad, then it has less money to advance in the fourth month: but that is all. Any loss which it may incur falls only on the firm or company itself. *Thirdly*, there is the Financial business. A financial company, pure and simple—that is to say, one which does not receive deposits, but trades only with its own subscribed capital—is likewise a simple, though always a risky business. It need not keep any reserve, so far as the public is concerned, for it has no liabilities to the public; and any losses which it may make, like those of a pure discount-establishment, produce no more serious result than a contraction of its business-operations.*

* A Financial company may safely receive deposits, and employ them in its business, provided those deposits are not "at call," but are borrowed for a comparatively long period. A bank, also, which has a large amount of deposits, may safely invest a portion of this amount in long-dated securities, seeing that some portion of its deposits may be reckoned upon as really not liable to be called for.

But all those three kinds of monetary business had become blended, or jumbled together, in 1866. Discount and Financial companies had invaded the province of Banking, by receiving deposits at call and at short dates; while banks sought to rival the profits of financial companies by advancing their money—to contractors and others—for long periods, and in some cases also upon precarious securities. Hence, when a distrust of the Financial companies arose, the suspicion of rottenness, aggravated by the extensive "bearing" operations, quickly extended to all classes of monetary establishments.

Beyond this point it was madness. When distrust became panic, when the persistent sales and shameless slanders of the "bearing" confederates culminated in a general alarm and continuous run for deposits, the game was up. No bank can long withstand a continuous pressure of this kind. For example, the Bank of England itself (thoroughly solvent though it ever is) must have fallen if subjected to a demand for deposits as great in proportion as that which was made upon the Bank of London,—from which bank one-half of its deposits was called up at a swoop. Whether a bank fell, or whether it stood, during that terrible period of Panic, really depended not so much upon its substantial solvency, as upon the extent to which the current of panic set in strongly against it.

The great discount-house of Overend, Gurney, & Co. was the first which fell before the general distrust and the persistent "bearing" operations on the Stock Exchange. This establishment, at starting in its new

form as a Limited Liability Company (in August 1865), had locked up 2½ millions of its capital in the purchase (from the old private firm) of securities which could not be realised for a long time, and a large portion of which was worthless. When a distrust of finance-business began, this Company was immediately singled out for attack by the "bears," or "speculators for the fall:" the price of its shares was driven down, till the shareholders and customers of the establishment took the alarm; and a slow but persistent run for deposits was made upon it. At length it was forced to apply for assistance to the Bank of England; but as it had not an adequate amount of sound negotiable securities to offer, the Bank refused; in fact the Company was thoroughly rotten: and so, to the dismay of the City, "Overend, Gurney, & Co." closed their doors.*

We need not speak of the profound impression and widespread panic which the fall of this great establishment occasioned. We must proceed with the narrative. It was a run for deposits (of which Overend, Gurney, & Co. used to hold upwards of 12, and in the palmy days of the firm 18 millions) which caused the stoppage, —a run which not even the most prudently conducted establishment can long withstand. And a similar run, though of lesser extent, thereafter commenced upon

* Although this great establishment had been grievously mismanaged for some years before its fall, the great deficit in its assets compared to its liabilities, when wound up, was partly occasioned by the unprecedented depression of all kinds of property which *followed* the Crisis. And this is true in regard to the ultimate balance-sheets of all the companies which failed last year. Owing to the effects of the Crisis, their assets or securities did not realise anything like the amount which they would have yielded in ordinary times.

nearly all the monetary establishments in the City. The English Joint-Stock Bank, a considerable portion of whose deposits had been placed at interest with Overend, Gurney, & Co., at once closed its doors. At midday (12th May) the panic was at its height. Lombard Street was actually blocked up by crowds of respectable persons who thronged the doors of the banks and other establishments. Lothbury, Bartholomew Lane, and adjoining streets, were also thronged with excited knots of people. While depositors rushed to withdraw their money, a body of onlookers gathered before each bank or financial establishment, expecting to see it close its doors. Every one was on the alert for bad news, and discussed only too freely the dangers which threatened the various establishments. A list of the shareholders of the fallen firm of Overend, Gurney, & Co., published at the high price of one shilling, was eagerly bought up at 2s. 6d. The penny papers, in like manner, were bought at 3d.,—so great was the eagerness to hear the latest news or rumours. Consols were unsaleable: no one mistrusted their value, but there was no currency wherewith to purchase them. The Bank of England itself would not give loans upon them.

This was a striking proof of the severity of the monetary dearth. The Government Bank—the establishment which, on the average, gets the use of six millions of Government money free of interest—would not even make a loan upon the security of Government Stock! This was a strange proceeding: nevertheless there was a valid reason for it. Although the Bank is greatly favoured by the Government, an Act of Parliament has

placed a restriction upon its power of issuing notes. In cases where the Bank could extend its note-issues with perfect safety to itself and immense advantage to the public, the Act of 1844 prevents its doing so. Hence, so long as the Act of 1844 continued in force, the Bank was quite entitled to say: "No, we cannot lend our notes upon consols, because we may need those notes in payment of our own deposits. And for the same reason, we cannot assist any embarrassed company, howsoever solvent it be, and howsoever disastrous to the community will be its fall."

More money was wanted by the community in payment of deposits: and where was the money to come from? Deposits were being called for in notes, and notes in sufficient abundance it was impossible to get. The whole amount of notes allowed to be issued in the United Kingdom hardly exceeds the amount of deposits in a couple of the London banks (the Union and the London and Westminster). The supply of currency was inadequate to the wants of the time; and hence the reserve of consols and other convertible securities which banks keep on hand to meet emergencies became of little avail. Although one or two of the banks had been conducting their business imprudently, the grand difficulty arose not from any want of assets on the part of the banks, but because it became wellnigh impossible for the banks to convert their assets into money.* The Bank of England is the great fountain of currency,—it is also the sole bank of issue in London; but when it was appealed

* In order to show the position of the London joint-stock banks, we subjoin a statement of their Liabilities and of their Reserves, as

to for a supply of notes, in exchange for securities which it would readily have accepted in ordinary times, it declined to part with its notes. Its power of issue was restricted by an Act of Parliament; and on that "black Friday" it had no more money on hand than was necessary for its own safety. In fact, if on that day the Bank of England had been subjected to a run for deposits, like that which was made on many of the other banks, it must have stopped payment. When it shut its doors on that day, its reserve of notes had fallen so low that the amount would have been cleared off at the first rush, if a run for deposits had been made upon it.

Banks, discount-houses, and financial-companies, all were striving to convert their assets into currency, in order to meet the unusual demand made upon them by

given in the report of those establishments for the half-year immediately preceding the crisis of 1866 :—

	Liabilities to the Public.	Reserve.		Total.	Ratio of Reserve to Liabilities.	
		Cash.	Stock.		Cash Reserve.	Total Reserve.
	£	£	£	£	percent.	percent.
London & Westminster,	20,779,301	1,677,841	2,489,412	4,167,253	8.07	20.05
London Joint-Stock, .	18,215,358	867,191	1,020,000	1,887,191	4.76	10.36
Union Bank, ...	17,794,263	2,816,994	1,458,825	4,275,819	15.08	24.03
London & County, . .	12,851,815	2,907,992	1,141,481	4,049,473	22 62	31.50
City Bank, ...	4,859,720	579,448	300,943	880,391	11.92	18.11
Bank of London, . .	4,335,377	820,497	227,167	1,047,614	19 01	24 16
Consolidated Bank, . .	3,818,000	718,111	117,036	835,147	18.83	21.09
Alliance Bank, . . .	2,504,168	435,930	100,000	535,930	17.40	21.04

From these statistics it appears that the two banks which fell, the one temporarily and the other permanently (viz., the Consolidated Bank and the Bank of London), held a larger reserve than any of the other banks, except the London and County. This is the simple fact: at the same time it must be borne in mind that the reserve of a very large bank need not be so great in proportion to its liabilities as that of a minor bank should be.

their depositors, while the supply of banking-currency, as restricted by the Act of 1844, had reached its utmost limit. The deposits of the country, whether stored in banks or in other monetary establishments, amount to about £400,000,000, while the amount of banking-currency is only about £40,000,000: moreover, only half of this amount is available as a reserve for all the banks in the kingdom,—the remainder being absorbed in the active circulation of the country. Hence, when a panic occurs, and an extraordinary demand for deposits takes place, there is no adequate means of meeting that demand. The banks cannot meet the requirements of the community. On that memorable Friday, two millions of banking-currency (notes) were paid across the counter of one of the most powerful and best-established banks in London; and a similar run was made on several other banks. It was impossible long to withstand such a run. Another day of similar panic, and every bank and monetary establishment in London must have stopped payment.

The panic was at its height at midday. Shortly before one o'clock, the second edition of the daily papers appeared, containing an announcement that the Bank Act was suspended. A salutary change immediately became visible: Lombard Street became passable, and the crowds in the adjoining streets diminished. The run slackened,—but the announcement was premature. The Bank Act was not suspended; nor indeed, at that time, as appears from the subsequent statement of the Chancellor of the Exchequer, had the Government given any attention to the matter. In this emergency a depu-

tation from the joint-stock and private banks was despatched to apprise the Government of the state of matters in the City, and to urge the immediate suspension of the Act of 1844. In the City, the managers and directors of banks and of other monetary establishments remained at their post till past midnight, anxiously receiving the tidings of disaster, and waiting for the announcement of the suspension of the Act.

It was midnight before the announcement was made. In the interview which the deputation from the banks had with the Chancellor of the Exchequer, the necessity for suspending the Act was urged upon the Government by all present, except the representative of the Bank of England. This was mere bravado on the part of the Bank. The other banks could have shut it up at once, simply by withdrawing the reserves which they keep at the Bank. Indeed one of the representatives of the joint-stock banks is reported to have said plainly, addressing the Bank's representative, — "I can draw a couple of cheques to-morrow morning which will shut you up at once." The Bank Directors knew this quite well; but they knew also that they could indulge in bravado safely, as it was perfectly certain that the Bank Act must be suspended. The Chancellor of the Exchequer saw this plainly enough, and the Act was suspended accordingly,—for the third time, although it had only been in existence for twenty-two years.

The effect of the announcement of the supension of the Bank Act was so salutary that next day (Saturday) it was generally thought that the crisis was at an end. But, as became visible in a day or two, the crisis was

not at an end. Why? The Government had suspended the Act, the artificial restriction upon the supply of banking-currency, in order to meet the unusual monetary requirements of the public; but the Bank of England, to which alone was given the power to extend its note-issues, declined to avail itself of the power thus conferred upon it. It refused to extend its note-issues beyond the amount permitted by the Act of 1844. It would have done so readily to save itself, but it refused to do so for the purpose of relieving others.

The result of such a course was, of course, disastrous. The crisis continued, the panic revived. Large commercial failures began, imperilling the banks which held the bills of the fallen merchants; the "bearing" operations went on; a run for deposits was kept up on several of the banks. It was impossible for those establishments to convert their securities into bank-notes in sufficient amount to meet the run upon them. After paying out fifty per cent of its deposits in cash, the Bank of London (a substantially solvent establishment) had to stop: as almost every bank in like circumstances must do. When the Bank of London stopped, the Consolidated Bank came to the rescue. An arrangement was made by which the Consolidated Bank took over the business of the fallen bank: engaging to pay its current and deposit accounts on demand, and also to carry on its discount-business,—a great boon to the customers of the suspended bank, and also a measure well calculated to allay the panic. But as the Consolidated Bank did not engage to take over the "acceptances" of the Bank of London, the legality of the

arrangement between the two banks was challenged, and the Consolidated Bank was threatened with a suit in Chancery. Thereupon the Bank of England refused to give any assistance,—that is to say, it refused to make advances to the Consolidated Bank on securities quite as good as those which it was discounting for its own customers. In these circumstances, the Consolidated Bank was unable to meet the run upon it: and after paying out a large sum to the depositors of the Bank of London as well as its own, during a struggle of three days, it closed its doors. After a still longer struggle—and mainly in consequence of a lying telegram sent from this country to Bombay, announcing its failure—the Agra and Masterman's Bank was likewise compelled to suspend payment.*

Contemplate the magnitude of the disaster. Overend, Gurney, & Co., the oldest and most powerful discount-house in the kingdom,—the English Joint-Stock Bank, which fell because a large portion of its deposits was locked up by the stoppage of Overend & Co.,—the Imperial Mercantile Credit Company, the European Bank, the Bank of London, the Consolidated Bank, and the Agra and Masterman's, with its widespread connections, were wrecked during that terrible season of panic.

* All of those three banks—the Bank of London, the Consolidated, and Agra and Masterman's—were perfectly solvent establishments, and the two latter subsequently resumed business. Their suspension (which was only momentary in the case of the Consolidated Bank) was caused not by a want of assets, but from the impossibility of converting their assets into currency (Bank of England notes) in order to meet the unusual demand upon them.

Those establishments used to hold about thirty millions of deposits, and made advances on bills, &c., to the trade of the country to a like extent. Their stoppage accordingly created a vast and twofold embarrassment. The depositors with those establishments could not get the use of their money, and the commercial customers could not get their usual advances. The deposits in those establishments had been greatly reduced by the persistent run upon them, but, at the time of the stoppage, they still amounted to about sixteen millions. This immense sum (although every shilling of it would ultimately be repaid, with interest) became temporarily unavailable to its owners. Not a shilling of it could be repaid until after the tedious delays of a judicial liquidation. Meanwhile, what were the owners of that deposited money to do? No one nowadays keeps more than a few pounds in hand—seldom enough for a single day's expenditure, — the cheque-book being used in payment of all sums above £5. Hence, for bare existence' sake, these depositors required to get loans from some quarter or other, to compensate the lock-up of their own money. But where, in that season of panic, were such advances to be got? All the banks (with the exception of the Bank of England, in whose favour the Act of 1844 was suspended) were nearly drained of currency, by the run for deposits which had taken place. Nor could these banks venture to lend out as usual the little money which they held, fearing lest a fresh run for deposits might be made upon them. The consequence was, that those banks were not able to make the usual advances to their own customers,—much less to

the unfortunate depositors in the suspended establishments, who could get no assistance, even upon the best securities, except by applying to the Bank of England. The discount-customers of the suspended establishments were in the same predicament. Their only chance of obtaining the customary advances, indispensable to the carrying on of their business, was by applying to the Bank of England.

In this way the Bank at once obtained an immense addition to its business.* All the discount-business of the suspended establishments came to it, as well as a considerable portion of the depositors with those establishments, who required loans to compensate the lock-up of their own money. What is more, all the money in the hands of the suspended establishments was, according to law, transferred to the keeping of the Bank of England. And this money the Bank could lend out freely, to the last shilling,—for this money was not liable to be called for by its owners until after the judicial liquidation of the fallen establishments had commenced. All this was a windfall to the Bank of England. It not only obtained an immense addition to its loan-business, but also a great addition to the money deposited with it,—which money it could use freely in carrying on this extension of its business. The Bank, in fact, became possessed of the monetary assets of the suspended establishments, free of all immediate liability to repayment: while the depositors with those

* The loans and discount-business of the Bank at once increased 10 millions, or 50 per cent; fully 5 millions were added to its private deposits, and nearly 4 millions to its note-issues.

establishments (the rightful owners of that money) had to come to the Bank begging for advances. Thus the Bank, in so far as it granted any of those advances, was simply lending to these unfortunates their *own money* at an exorbitant rate of interest!

In these circumstances, what was the conduct of the Bank? It is, or at least it regards itself, as a private establishment, and it acted accordingly. By the fall of many of its rivals, and by the embarrassment of others, the Bank got an immense accession to its business; and it kept that business to itself as long as possible, —at the same time charging thereon the highest possible rates. Both of those objects were attained by the exorbitant rate which it charged for the loan of its money, and by its refusing to make advances save upon the very best and short-dated securities. The effect of the panic (as we have said) was to occasion a dearth of currency: the statutory supply of currency became inadequate, owing to a sudden increase in the monetary requirements of the community. And the Act of 1844 was suspended in order to allow this want to be supplied. But the power of supply was vested solely in the Bank of England: and the Bank was niggardly in its use of the power conferred upon it. Probably the Directors thought it would be a slur upon the Bank's credit for it to make use of the extended power of issue conferred upon it by the supension of the Bank Act. But, in any case, it was for the Bank's interest to keep the supply of currency inadequate: and it did so. A Bank-rate of 10 or 12 per cent means panic: and the Bank charged those rates. The result was

that the prevalent disquiet was prolonged. Large commercial failures took place; thereupon the banks which held the bills of the suspended firms encountered a new embarrassment, and were exposed to fresh distrust on the part of the public; and, so circumstanced, they could not venture to lend their money freely, lest it should suddenly be needed to meet a run for deposits.

In this way the Bank had the field to itself. In proportion as its rivals had to suspend, the more deposits and discount-business came to it. Moreover, as long as the surviving banks remained embarrassed by fear of the panic, the Bank got a portion of *their* business also. Hence—as the Bank considers itself entitled to act simply as a private establishment—it had an ample motive for declining to avail itself of the powers conferred upon it by the suspension of the Act of 1844. Had the Bank at once used those powers freely, and exceeded its statutory issues to the extent of even two millions, the 12th of May would have been the last day of the panic. The crisis would have subsided; the Bank of London, the Consolidated Bank, and Agra and Masterman's (all of which, we repeat, were solvent establishments), would have stood; and hardly any commercial suspensions would have taken place at all. But in such circumstances the other banks would have been able promptly to resume their ordinary operations, and the rate of discount would have fallen to something like its ordinary level. The Bank of England would not have reaped so great a harvest at the expense of the community and of the other banks. Obviously, it is much more profitable for the Bank to issue (as it did)

25½ millions of notes at 10 per cent than to issue 28 or 30 millions at 5 per cent.*

The Act of 1844 was suspended *pro bono publico.* The suspension was not made merely for the sake of the Bank of England,—much less for the sake of increasing the profits of the Bank at the expense of the other monetary establishments and of the community at large. A suspension of the Act, under any circumstances, is of great service to the Bank. It relieves the Bank from the artificial restriction imposed upon its note-issues (which are never, and never have been, distrusted), and thereby frees it from its liability to an artificial bankruptcy. During the panic of 1866 the Bank of England was actually as liable to a failure of this kind as were the other London banks. A large portion of its deposits consists of the cash-reserves of the other banks; and on the 12th of May any one or two of those banks, simply by demanding payment of their own money, could have made the Bank insolvent. In this respect the suspension of the Act was called for in the interests of the community, and also as an act of justice to the Bank itself.

But it is a crying evil of our present monetary system that a suspension of the Act, in the mode which has hitherto been adopted, is an injustice to all the other

* The Bank's net profit on the half-year ending on 5th September 1866 amounted to £975,655, the largest ever made by the Bank. Moreover, if the weekly gains of the establishment be examined, it will be found that these were fully twice as great during the period of monetary distress as in the remainder of the half-year. During the fourteen weeks when the rate of discount was 10 per cent, the Bank's profits were £679,000, against only £300,000 in the other twelve weeks, when the Bank-rate ranged from 6 to 8 per cent.

banks and monetary establishments, as well as to the mercantile community. It immensely increases the monopoly possessed by the Bank. The Act, in fact, is suspended only *quoad* the Bank of England. Upon all the other banks of the country the restrictions of the Act are kept in force. However great may be the want of currency, none of the other London banks are allowed to issue notes upon any terms; and the 210 banks of issue in the United Kingdom are in like manner forbidden under any conditions to exceed the limitation imposed upon them by the Act. The effect of the suspensions of the Act, as hitherto carried out, is a special act of favour to the Bank of England,—an addition to the privileges, a completion of the monopoly, conferred upon it in past times.

The monopoly of a purely State Bank (if such an establishment be practicable) would be intelligible: for, *ex hypothesi*, such a bank would have no interests of its own: it would have no shareholders, no private proprietary, no dividends to make: in fact, it would have no interest in making profits at all, seeing that such profits would be simply a tax upon the community. But to confer special privileges upon a private bank is an injustice to all other banks and to the community at large. And to suspend the law in a way which only increases the monopoly of such a bank, while maintaining the legislative restrictions upon all other banks, in principle is monstrous, and in practice is most inimical to the interests of the community. The Directors of the Bank of England are men of honour and integrity; but even if they were patriots of the purest type—if they

held themselves bound to use the additional privileges conferred upon them by the suspension of the Act wholly and solely in the interests of the community,—the power conferred upon them would be invidious, and too great to be intrusted to any body of private individuals. But the Directors of the Bank of England make no such incredible professions of disinterestedness. They avow openly that the Bank (although largely favoured by the State) is a private establishment; that they are responsible only to their shareholders; and that the chief rule of their conduct is to manage the Bank as profitably as possible.

It is a loss to the community that solvent banks and monetary establishments should fall; but it is pure gain to the Bank of England. Not only are so many rivals thereby swept permanently out of the field, but the immediate result is to add greatly alike to the deposits and to the discount-business of the Bank. Manifestly such onesided suspensions of the Act of 1844 as we have now thrice witnessed are inadmissible, intolerable. They bolster up the reputation of the Bank of England (which under a natural system would need no bolstering) to the disadvantage of the other banks; and, at the same time, such suspensions of the Act confer upon the Bank a complete monopoly of the currency,—they confer despotic and irresponsible power upon a private establishment which confessedly makes use of its privileges with a view to increase its gains.

The reasons for the suspension of the Bank Act were obvious. Owing to the panic and consequent run for deposits, there was a sudden increase in the monetary requirements of the public; and it was impossible for the

banks and financial establishments to meet this demand, as they had no adequate means of converting their assets into currency,—the amount of banking-currency being artificially restricted by the Act of 1844.* Nevertheless the suspension of the Act was made in such a way as to give to a single bank the sole power of supplying the extra amount of currency required.

We have seen the motives of self-interest which this privileged bank (the Bank of England) had for refusing to avail itself of the power conferred upon it by the suspension of the Act of 1844. The greater the dearth of currency, the higher the price which the Bank could obtain for the issue of it. Let us now consider the other side of the question. Let us see if there were any prudential considerations, connected with its own solvency, which can be urged in justification of the course which was adopted by the Bank.

The only effect which any bank has to fear from an unusual extension of its note-issues is, that the public may lose faith in the notes, and demand payment of them in specie. Well, has the public ever lost faith in the notes of the Bank of England, and made a run upon the Bank for payment of its notes in coin? The answer is, *Never*. Not only during the present century, but for wellnigh a hundred and fifty years, the Bank's notes have never once been distrusted. Even in 1825, when the wildest panic existed, the notes were in as good repute

* It was stated by Mr Clay, in the debate of 27th February last, that owing to the spread of false rumours, one of the first-rate London banks had to incur a loss of £70,000 during the panic of 1866, in converting a portion of its assets into banking-currency—*i.e.*, Bank of England notes. Of course, the less powerful banks fared worse, as the Bank of England then refused to give its notes in exchange for securities such as it gladly accepts in ordinary times.

as ever. Then, as now, owing to the panic, there was an unusual requirement on the part of the public for currency; and the moment the Bank changed its policy, and instead of restricting its issues, and contracting its loans, lent out its notes freely to supply the requirements of the public, the panic was at an end. What is more, the note-issues of the Bank at that time rose to as high a point as they did during the recent panic (25½ millions), although in 1825 there was a great drain of gold for export, and the specie in the Bank had fallen to one million.

During the recent panic, on the contrary,* there was

* The following table shows the movements of specie and the Bank's charge for discounts during the most critical months of 1866 :—

Week ending	Imports of Gold.	Exports of Gold.	Gold in the Country.		Gold in the Bank.	Bank-rate.
			Increase.	Decrease.		
Mar. 7	120,366	41,254	79,112		14,050,504	7
14	229,528	17,985	211,543		14,327,618	6
21	70,684	20,960	49,724		14,455,523	
28	520,299	2,948	517,351		14,362,397	
Apl. 4	332,577	22,393	310,184		14,251,947	
11	60,277	41,769	18,508		14,234,118	
18	300,671	200,583	100,088		13,889,112	
25	124,866	128,403		3,537	13,855,771	7
May 2	140,489	242,973		102,484	13,509,140	8
9	44,925	102,347		57,422	13,156,140	9
16	328,824	132,435	196,389		12,323,805	10
23	364,164	237,686	126,478		11,857,786	
30	1,050,708	1,134,232		83,424	11,878,776	
June 6	2,034,102	365,119	1,668,983		13,278,961	
13	2,395,584	992,900	1,402,684		14,481,895	
20	1,347,317	811,319	535,998		14,851,120	
27	1,500,454	1,289,421	211,033		15,042,399	
July 4	414,333	568,187		153,854	14,876,947	
11	71,859	697,994		626,135	13,993,470	
18	704,674	246,738	457,936		13,645,975	
25	1,174,486	798.541	375,945		13,716,829	
Aug. 1	569,211	402,321	166,890		13,793,340	
8	459,988	376,860	83,128		13,622,429	
15	469,919	407,226	62,693		14,150,956	8
22	433,050	99,820	333,230		14,772,220	7
29	1,170,251	112,386	1,057,865		15,320,020	6

no drain of specie for export, and the Bank's stock of gold was twelve millions. Nevertheless, the notes of the Bank circulated as freely during the panic of 1825 as they did during the panic of 1866. Neither in the one case nor in the other was there the least distrust of the Bank's notes, nor any demand on the part of the public for payment of them in specie. The amount of the Bank's note-issues in 1825 and 1866 was the same, while the Bank's stock of gold was twelve times as large in 1866 as in 1825. Since, then, the notes of the Bank were never distrusted or cashed in 1825, who believes that there was any risk of its notes being distrusted or cashed under the vastly more favourable circumstances of 1866? In fact, it is a special feature of the panic of 1866 that the notes of no bank were distrusted. Not only the notes of the Scotch and Irish banks, but the notes of the two hundred provincial banks of issue in England, circulated as freely as before*—and yet the issues of those English banks of issue are totally unprotected by any security required by Government.

There is another matter in connection with the suspension of the Bank Act which claims special notice. It has become a stereotyped practice, when such a suspension takes place, for the Government to stipulate that the Bank shall charge an exorbitant rate from the community upon the extra note-issues which at such times are imperatively needed, and at the same time

* As it has been alleged that the increased demand for notes from the Bank of England was partly occasioned by the notes of the other English banks of issue falling into discredit, we shall show the true facts of the case in the Appendix.

to appropriate the profit upon these extra note-issues to the State. The latter provision is essentially illusory: for the trifling gain so made by the State is dearly paid for by the community. This provision, in fact, simply gives the Bank an additional motive of self-interest for restricting the supply of currency to the statutory amount, and thereby making larger profits than would otherwise be possible. In the panic of last year the Bank declined to make those extra issues (£2,000,000)—which it was authorised to make, but upon which it was to get no profit,—while it willingly kept its charge for banking-accommodation at the exorbitant rate prescribed by the Government. Despite the power conferred upon it to extend its note-issues in order to meet the urgent requirement for them, the Bank never at any time exceeded its statutory amount of issue. By so doing it obtained a larger amount of profits than if it had issued to the full extent of the powers conferred upon it.

But upon what ground does the Government, when the Bank Act is suspended, enjoin that the exorbitant rate of 10 per cent shall be charged upon the extra issues of currency required by the community? Is it afraid that the Bank, which has then an absolute monopoly of the currency, will forget its own interests, by charging too little for its loans? The idea is preposterous. The only effect of such a stipulation is to nullify the very object for which the Act is suspended. The suspension takes place only when the statutory amount of banking-currency becomes confessedly inadequate to the wants of the community; and for the Government

to decree that an exorbitant rate shall be charged upon the extra issues required, and to appropriate the profit on them, is simply to undo with the one hand what it does with the other. It gives the Bank an additional motive *not* to meet the wants of the public,—*not* to make the extra issues of currency which the public require, and for the sake of supplying which the Government suspends the Act. Such a procedure is as absurd as if the Government were to fill a reservoir for the use of the community, and were simultaneously to narrow the orifice,—so that the community should get no more water than before, while paying a double price for it.

Moreover, what was the good of a high rate of discount during the panic of 1866? As long as the Act of 1844 is in force, the Bank may say—"We are allowed to issue only a certain amount of notes, and as we have a greater demand for these notes than we can meet, we shall lend them only to those who are willing to pay the highest price for them." This is intelligible,—although the system under which such a case can arise is obviously unnatural and vicious. But when the supply of currency is allowed to take place freely, by the suspension of the Act, what object does an exorbitant Bank-rate serve? None at all: except to increase the profits of the Bank at the expense of the community, and to the detriment of the trade and industry of the country.

Theorists, indeed, whose dogmas have inflicted dire calamity upon the country during the last quarter of a century, have proclaimed with extraordinary assurance that a high bank-rate serves immediately to attract specie from other countries. But, in the first place,

during the crisis of 1866, there was no want of gold at all. At the worst point of the crisis, there were twelve millions of gold lying idle in the Bank, and no one ever asked for it or wanted it. Whatsoever, then, was the object of the exorbitant bank-rate of 10 and 12 per cent, this high charge for banking-accommodation was certainly not needed for the purpose of attracting gold from abroad. There was quite as much gold as we required: at least twelve millions more than anybody asked for, or wanted. Secondly, as experience shows, the idea that a high bank-rate is a potent means of attracting gold from other countries is erroneous.* The influence of a high bank-rate on the efflux and influx of specie is almost inappreciable. If a country has to make larger payments abroad than the amount of foreign bills which it holds, abroad gold must go. In like manner, if the balance of its trading and financial operations is in its favour, gold will pour into the country, however low may be the rate of discount. In October 1865, Baron Rothschild confidently declared, before the French Government Inquiry into Banking, that if the Bank of France were to allow its rate of discount to fall two or three per cent below that of the Bank of England, or of any other foreign bank, the result would be that the Bank of France would be drained of its whole amount of specie. Nevertheless, during the critical ten months which followed, the rate of the Bank of France was on the average fully three per cent below that of the Bank of England; yet its stock of specie, so far from being drained away, increased rapidly, while the specie in the

* See also *supra*, pp. 166-8.

Bank of England during those months did not increase at all. In truth, during the months of May, June, and July last year, the bank-rate in England was 10 per cent, while the bank-rate in France was only 3½ and 4 per cent, and yet the specie in the Bank of France continued steadily to increase.*

Facts are the only sure teachers; and these facts, as well as experience on many other occasions, demonstrate conclusively the impotency of a high bank-rate to attract specie from other countries. Moreover, by producing a panic, a high bank-rate actually creates or intensifies an external drain upon the banks,—as in the case of last year, when it produced an increased export of specie by throwing discredit upon our commercial bills,—an effect which Lord Clarendon's circular despatch was totally impotent to prevent. And finally, a high bank-rate, by producing failures and panic, creates an internal drain of specie also. In truth, while a high bank-rate is practically useless in attracting specie from other countries, it is the most potent means of producing panic and disaster. It is the sure parent of commercial crises, and sometimes also of banking crises.

As regards our monetary system, the grand lesson of the late Crisis is as obvious as it is important. To rigidly fix the amount of banking-currency in any country is an absurdity. The monetary requirements of a country steadily increase with the increase of trade and population; they are also liable, from many causes, to sudden and great fluctuations. The run

* For a detailed statement of these and other monetary statistics of the Crisis of 1866 we refer the reader to the Appendix.

upon banks in a time of panic, for example, constitutes a sudden increase in the requirement for currency; and this can only be met by a corresponding increase in the supply. During the crisis of 1793, the Government came promptly to the rescue, by offering a supply of Exchequer currency upon the security of goods—property of *any* kind. Five millions of this kind of currency were voted for the supply of all solvent firms who should make application for it, — and thereupon the panic disappeared as if by magic. In 1825, when a great run upon the banks took place under the influence of panic, the difficulty vanished the moment the Bank of England declared that it would supply currency freely, by making advances upon any kind of good security which was offered to it.

Without such measures, in times of panic, not only Trade but the whole banking-system of the country is liable to come to the ground. During a run for deposits, the amount of the assets held by the banks are of no use if they cannot be converted into currency. A depositor will not accept payment in commercial bills or suchlike securities, howsoever valuable these may actually be: they must be turned into money before they can be used by the bank in payment of its liabilities. And, under our present laws, as has now been proved for the third time, such a conversion of banking-assets into currency, in times of crisis, cannot take place in any degree commensurate with the requirements of the banks and the public. During the late Crisis, the grand defect of our monetary system was, that assets were not convertible into currency. Money's worth could not procure money.

XV.

IMPOLICY OF THE BANK ACTS

Such is the working of our present monetary system, alike in fair weather and in storm. It is admitted even by the supporters of the system, that some of the provisions of the Bank Acts are absurd and exceedingly injurious. The *Economist,* a most able and influential journal, is of this opinion. Yet it shrinks from proposing to abolish the Act of 1844. It says that if the Act were abolished, the Directors of the Bank of England would be left free to act as they like; and also that the Directors themselves do not desire to be released from their fetters. Why should they? The Act, as we have shown, is a most potent means of increasing the gains of the Bank,—the tendency of its provisions is to make the rate of discount in this country steadily rise. And, moreover, the Directors make the Act a convenient excuse for their exorbitant charges, even when their conduct has no necessary connection with it. They make the Act a vague but most efficacious shield, which

they interpose between themselves and the protests and criticisms of the public.

As to the alleged peril of leaving the Bank Directors to act as they like, what does it mean? The Directors act as freely (in all respects save one) under the Act, as they ever did without the Act. The only provision which the Act imposes upon them is, that six or seven millions shall be locked up idly in the Issue Department. This large amount of specie they are not allowed to make use of in any way. This is the sole obligation imposed upon the Directors by the Act: and it is a provision alike noxious and absurd. To this enactment the Directors make no objection. One-half of their usual stock of gold being nullified, they charge a double or triple price for the remainder. As is well-known, when an article of indispensable use becomes scarce, a small deficiency of supply occasions a famine-price,—the price increasing in geometrical ratio to the actual deficiency. The Directors, in fact, can eat their loaf and have their loaf. They can have their six or seven millions of gold locked up, and yet make larger profits than if they had the use of it. To the community, the case stands thus:—when there are 14 millions of gold in the Bank, the Bank must act as if there were only seven. And the Bank charges fully twice as much for the use of those seven millions as it would or could do if the whole 14 millions of specie were at its disposal. Moreover, this locking-up of nearly seven millions is intensified in its operation by the provision of the Act which forbade any notes above 14 millions to be issued save upon gold. If those seven millions of specie were simply locked

up, the evil would be less than it is. For what the country chiefly wants is not gold, but notes. But, while locking-up this large amount of gold-money, the Act at the same time forbade the Bank to issue notes in answer to the requirements of the community,—making its note-issues above 14 (now 15) millions entirely dependent upon the amount of gold in its vaults. Thus the Bank Acts impose an artificial restriction upon the Bank's use of its gold, and also upon the currency of the country. But the less adequate the currency, the greater the profits of the Bank which issues it. For example, when the Bank lends 19 millions at 9 per cent, its profits are double what they would be if the Bank's note-issues and rate of discount were at the usual amount—*i. e.*, 21 millions of notes lent out at 4 per cent.

This, then, is the sole provision of the Bank Acts which restricts the power of the Directors. And its effect is to raise the rate of interest throughout the country: to make money artificially dearer than would be the case if no such enactment existed. As the Bank is a private establishment, whose only object is to make its profits as large as possible, surely no legislation was needed in order to induce the Directors to charge a higher rate of profit than they would otherwise have done. In France and Belgium, an exactly opposite course has been followed: in each of those countries the Government, while conferring a monopoly upon the Bank, has wisely taken care to prevent the abuse of that monopoly, by preventing the Bank from increasing the rate of discount exorbitantly for the purpose of adding to its gains.

In all other respects, the Directors of the Bank of

England act as freely as if there were no Bank Act in existence. This is shown to demonstration by the fact that they now work the Act in an entirely opposite manner from that which was contemplated by its framers. Sir Robert Peel, Mr Goulburn, and the other authors of the Act of 1844, held that the only proper course for the Bank to take, when a drain of gold occurred, was to contract the currency,—to reduce its note-circulation. Sir Robert Peel even thought it a possible contingency (which he provided for) that the Bank might at certain times require to contract its note-circulation to eleven millions! This was an absurdity; but it was in perfect accordance with the erroneous notions upon which the Bank Act was founded. These notions are now wholly exploded: the Bank ignores them, and even the stanchest supporter of the "bullionist" doctrine admits them to be untenable. Nevertheless, the Act which was the offspring of those notions remains! Such is the strength of inertia, of the reluctance to change, in the English mind: an influence greatly enhanced by the fact that hitherto the only men who have been listened to as authorities on this subject are bankers and capitalists,—the very class of men whose personal interests are involved in keeping the rate of interest at the highest possible elevation.

An Act certainly must be of little use in guiding the conduct of the Directors when they act in direct opposition to the views and intentions of the framers of the Act. But let us show other instances of the freedom of action —we might say licence—on the part of the Bank Court. So far as the principle and provisions of the Act are con-

cerned, the Directors might have continued to charge the same rate of discount under the Act as before. Neither Sir R. Peel nor any of the framers of the Act contemplated any change in the price which the Bank charged for its discounts. Their idea was, as we have said, simply that when a drain of gold occurred, the Bank should contract its note-circulation; they neither enjoined nor desired that the Bank should at such times charge a higher price for its usual accommodation to the public. But the Bank now does the very reverse of this: it issues as many notes as usual, but charges a higher price for the use of them. Whenever a demand for gold in payment of its deposits takes place, the Bank raises the rate of discount, and in this way converts its own difficulties into a means of greatly increasing its profits. Instead of being guided by the principle upon which the Act was founded, the Bank totally repudiates that principle. At the same time, being now free from the fear of competition, by which it was partially kept in check previous to 1844, the Bank raises the rate of discount exorbitantly upon the most trifling pretexts.

Moreover, not only do the Bank Directors work the Act in a contrary spirit to the principle upon which the Act was based, but they have altered, and are constantly altering, their own action. Until eight or ten years ago, when there were twelve millions of gold in the Bank, the bank-rate was little more than half what it is now in similar circumstances. By the simple *fiat* of the Directors, the rate of discount has, in these circumstances been nearly doubled. Moreover, the Directors now treat a home-drain of specie just as if it were a drain

of gold for export; and, also, they treat a demand for notes just as if it were a demand for specie. Again — as has already been shown — they no longer tide over our quarterly and other periodical demands for money (as used always to be done in former times), but treat them as if they were permanent drains,—raising the bank-rate and thereby increasing their profits.

Again, since 1858, the Bank Directors have refused to give any accommodation to the discount-houses, by occasionally re-discounting (as they used to do) the bills held by those establishments. As a private establishment, the Bank has a right to act thus; but the procedure is questionable when it is considered that the Bank has been intrusted with a virtual monopoly of the supply of currency. Right or wrong, the result is to give another advantage to the Bank. Whenever a crisis of any kind occurs, the discount-houses have to stop their usual advances to Trade altogether: and the result is to secure for the Bank, at such times, the whole business ordinarily carried on by the discount-houses. In fact, when a crisis occurs, the Bank has now an entire monopoly of the discount-business: for the other London banks, although holding an amount of deposits nearly ten times larger than that of the Bank of England, have no power to issue notes,—they are entirely dependent on the Bank for the means (notes) of carrying on their operations: and accordingly, in times of great pressure, they cease to discount. In this way (speaking roundly) all the business goes to the Bank,—as was shown during the crisis in May 1866. The Bank has a clear field, and works its monopoly to the

full, at the expense of Trade and of the community at large.

Again, although the Act allows the Bank to increase its note-issues to any amount, on condition that it provides itself with a corresponding amount of gold, the Bank Directors make no effort to do so. As regards its supply of gold, the Bank maintains a purely passive attitude. If the bullion-merchants bring gold to it, good and well; if they do not do so, the Bank simply raises its rate of discount. Gold may be deposited with it, or withdrawn,—the Bank does not care. It takes no means to supply itself with specie, when more specie than usual is wanted by its customers: the only change which it makes is, to exact exorbitant rates from the public, and increase its gains without incurring any cost to itself.

Again, the Bank now keeps a large portion of its private securities in the form of railway-debentures, City bonds, &c., which necessarily have a long time to run before they are cashed. Such a locking-up of its capital creates a difficulty, and raises the rate of discount, whenever a time of pressure occurs. And as the *Times*, which justifies this procedure, admits, the Bank locks up its capital in this way because otherwise it would have to deal only in commercial and other bills, and thereby would have to reduce to a lower level the bank-rate, the charge for its accommodation to the public. This also is a procedure perfectly legitimate on the part of a private establishment, but which is open to criticism in the case of a bank which has a virtual monopoly of the banking-currency of the kingdom.

In fact, the Bank of England (although specially favour-

ed by the State) is, in its own estimation, and in point of law, purely a private establishment. It is important that this fact should be fully recognised. The Bank does not consider itself responsible as a conservator of public interests. In virtue of the Bank Acts, it possesses a dominating influence, a virtual monopoly of the currency; but it uses that monopoly, and is legally entitled to use it, as a private establishment, whose only object is to increase its profits by every possible means.

The Bank of England having shown the example of acting in this manner, all the other banks now closely follow its lead. Until of late years, the Scotch banks never used to charge the high rates adopted by the Bank of England; neither did the English provincial banks. But the Scotch banks now do this as a rule, and the majority of the English provincial banks do likewise. The same is true of the London banks and discount-houses. Knowing that their customers cannot get loans any cheaper at the Bank, those establishments usually charge the full minimum rate of the Bank of England. The only exception to this is, when the Bank's business is manifestly falling off, so as to indicate an immediate reduction of the rate; in which case, the other banks and the discount-houses usually "discount" the coming fall, and charge rather less than the Bank, in order to attract to themselves as many bills as possible before the rate falls to a lower point.

The two great evils of the Act of 1844 are these: Firstly, it fossilised the monetary system of this country. It stopped its growth,—it checked its natural expansion. With an ever-expanding Trade, we have a fixed Mone-

tary System. It is like planting a growing oak in a vase of iron. Secondly, the Acts established all the evils of a monopoly, without taking any means to prevent the abuse of that monopoly. They conferred a monopoly of the currency upon the banks of issue which were in existence in 1844,—of which the Bank of England (owing to the privileges which it had so long enjoyed) was the chief; and as regards England, the whole tendency of the Act is to intensify the existing monopoly, by fostering the Bank of England and checking the note-issues of all the other banks.

The twin systems of Restriction and Monopoly—restriction of the currency, and monopoly of the power to issue it—are sadly out of keeping with the times. The restriction amounts to a total prohibition of any increased use of paper-money in the form of banking-currency. *Mirabile dictu!* the principle of paper-money was repudiated by the Government of 1844: not a single bank in the country was allowed to employ it any further: and even the system of banking-currency as it then existed was seriously contracted. Had Sir Robert Peel and his advisers lived a century and a half earlier, they would have been found amongst the most bigoted opponents of the establishment of the Bank of England, —predicting, as many at that time did, the most woeful consequences to the community from the adoption of the system of banking-currency. And when beaten upon this point—as, thanks to the good sense of Parliament even at that time, would have been the case,—they would have been foremost in proposing for the Bank of England that monopoly which its founder openly

rejected, and which was also rejected in Scotland; but which, nevertheless, the Directors of the Bank of England ere long extorted from the Government in times of need by the tempting offer of loans.

In truth, the Act of 1844 is an utter absurdity. It has thrice broken down, after seriously injuring the community; and long ere this it must have proved absolutely unworkable but for the occurrence of two wholly extraneous events,—namely, (1) the unexpected discovery of the new gold-mines, and (2) the introduction in 1854 of the present "Clearing"-system. But for the new gold-mines this country could not have exported the 20 or 30 millions of specie now annually required to carry on our foreign trade;* still less could we have added so largely as we have done to our metallic currency, in supplement of our note-circulation. Moreover, even *with* the extraneous aid afforded by the new mines of California and Australia, the Bank Acts must ere this have proved unworkable but for the new system of "clearing" adopted in 1854,—whereby the

* The exports of specie during the last twenty-six years have been as follows (in millions sterling):—

	1841	'42	'43	'44	'45	'46	'47	'48	'49	'50	'51	'52	'53
Gold, . . .	·1	·5	2·3	·2	·2	·5	4·8	1·5	1·1	2·6	3·9	4·3	12·7
Silver, . .	3·8	3·5	3·0	3·4	3·8	2·4	3·8	7·0	7·7	4·4	5·0	5·9	6·1
Total, . . .	3·9	4·0	5·3	3·6	4·0	2·9	8·6	8·5	8·8	7·0	8·9	10·2	18·8

	1854	'55	'56	'57	'58	'59	'60	'61	'62	'63	'64	'65	'66
Gold, . . .	16·5	11·8	12·0	15·0	12·5	18·0	15·6	11·2	16·0	15·3	13·2	8·5	12·7
Silver, . . .	6·0	7·0	12·8	18·5	7·0	17·6	9·9	9·5	13·3	11·2	9·8	6·7	9·0
Total, . . .	22·5	18·8	24·8	33·5	19·5	35·6	25·5	20·7	29·3	26·5	23·0	15·2	21·7

From these statistics it appears that the exports of specie requisite for carrying on our foreign trade are now at least six times as large as they were in 1844.

settlement of balances between the London banks is effected by drafts upon the Bank of England, instead of by notes as before. In 1839 the transactions of the Clearing-House amounted to £954,401,000, and the amount of bank-notes required to settle those transactions was £66,275,000,—or nearly 7 per cent of the amount of the transactions. According to Mr Hankey, the transactions of the Clearing-House in the year ending 5th September 1866 were no less than £4,588,000,000, —or more than 4½ times as large as they were in 1839. Accordingly the amount of notes required to settle those transactions would, under the system as it existed in 1844, have been upwards of £300,000,000,—whereas, by the new system of clearing, not a single note is needed at all. But for those great changes—namely, the new gold-mines, and the new system of clearing—the Bank Acts must have become absolutely unworkable long ere this. Those Acts, in short, are alike erroneous in principle, disastrous in their operations, and thoroughly unworkable in any progressive country.

It is extraordinary to hear some people say, "Why should we abolish the Bank Act, when the Bank is quite content with it?" Well, so was Demetrius the silversmith with the worship of Diana. In both cases the object has been private gain. Never let it be lost sight of that the Bank of England is a private establishment. Not even in the worst dilemma that ever befalls the country does the Bank think of anything but its own interests. And these are, to keep the rate of discount as high as possible. All banks do the like. One may as well suppose that a farmer in a time of famine will

abate one iota of the price which he can get for his corn, out of deference to the sufferings of the community, as that a bank will not charge the highest possible price for its currency. The monetary monopoly established in this country in 1844 is the worst form of Protection and Monopoly that ever entered the head of a statesman to devise or of a people to acquiesce in. In principle, it is infinitely less defensible than the old Corn Laws. Apart from the fact that the Corn Laws were established for the purpose of preventing this country from being mainly dependent on foreign countries for its supply of food,—apart from the fact that the Corn Laws were supported on a very intelligible principle of State policy, favourable to the independence of the country,—even as a question of political economy, the system of Protection established by the Corn Laws was more defensible than the present monopoly of the supply of money. Under the Corn Laws, whenever the price of corn rose to a certain point, a supply of foreign corn was admitted at a merely nominal duty. It was only when the harvest was a bad one that the price of corn rose to this point: and the main effect of the law was to allow prices to rise to a point which would recoup the farmer for the deficiency of his crop,—his expenditure being as much in a bad harvest as in a good one.

An adequate supply of Money is as indispensable to our national prosperity, and to the employment of the working-classes, as a supply of Corn is to the life of the people. But under the present Bank Acts, the monopoly of the supply of money, the protective system established in favour of certain banks, has no limit

such as existed under the Corn Laws. However great may be the requirements of the community, the supply of money is restricted to a certain amount; so that, in times of pressure, the banks' charge for the use of their notes becomes exorbitant. In consequence, as trade and the monetary requirements of the country are yearly increasing, while the cheque-system has approached its full development, the rate of interest, the charge for the use of money on loan, is likewise increasing, and ever and anon reaches a most usurious point. A very trifling decrease in the ordinary influx of gold, or a very small increase in the demand for notes, sends up the bank-rate in geometrical proportion to the amount of the deficiency. A decrease of one-tenth in the Bank's stock of gold, or an increase of one-tenth in the demand for notes, sends up the bank-rate from 4½ to 8 or 9 per cent. And even when the Bank Act is suspended, the suspension brings comparatively little relief to the community. Practically the effect is simply to allow the Bank to carry on business at a usurious rate of profit—10 per cent. One might expect, indeed, that the Bank, when released from the legislative restriction upon its note-issues, would give some relief to the community by lowering its rate of discount. But the Government insanely (we can use no milder term) limits the relaxation of the Act in such a way that the Bank cannot, if it would, lower the rate. The Government says to the Bank:—"We authorise you to issue two millions of notes in excess of what the Act permits you to do,—for we see that if this is not done, such a panic will arise as will break down our monetary system altogether: but

at the same time 10 per cent shall be your lowest charge upon your accommodation to the public: and, moreover, all the profit upon these extra two millions of note-issues shall go to the State."

What is the meaning of this? In 1857 this strange procedure was adopted by the Government simply because it had been adopted in 1847: and in 1866 out of deference to those precedents. But if we ask why was such a course adopted in 1847, no answer comes back to us. If the Government, acting in the interests of the public, were to say to the Bank,—"We have a right to all the profits on those extra issues, but we shall waive this right on the condition that you lower your rate, that you reduce your charges to the public," the procedure would be intelligible. Instead of increasing the demand for notes, this procedure (as abundant experience shows) would, by restoring confidence, actually lessen it. But according to the present system, when the Government relaxes the law, by suspending the Bank Act, it orders an exorbitant rate to be charged by the Bank (as if the Bank required any extraneous impulse to do this!), and at the same time appropriates to the State the trifling gain upon the Bank's extra issues, at the expense of prolonged troubles and tremendous losses on the part of the community. This procedure—to borrow another illustration from the corn-trade—is as if the Government, in a time of famine, were to allow two or three million quarters of wheat *only* to be imported; were to forbid these to be sold except at a famine-price; and also were to appropriate the profit on the sale thereof to the State. The consequence would be

that the corn-merchants would not care to import at all, —because they could get no profit on the transaction; moreover, if the corn were imported, the farmers would get the same famine-prices for their corn just as if no importation had taken place. If, when the price of wheat is £5 the quarter, the Government were to allow two million quarters to be imported, but no more, and only on condition that this imported corn be not sold below the previous price (£5), and that the profits on the sale of it should go to the State: this would be an exactly parallel case to what occurs under our monetary system when a crisis occurs and the Bank Act breaks down.

What is more, under the Corn Laws, protective as they were, the business of corn-growing in this country was not a monopoly: on the contrary, those laws gave every possible encouragement to the growth of food for our people. Any one could grow corn who pleased. As much capital might be invested in the business as the community desired. So that, if more corn-growers were wanted, and competition were desired, this would naturally take place. But no such freedom of trade exists in the supply of banking-currency,—which, nevertheless, is as needful to our trade as corn is to the life of the people. The banks of issue which existed prior to 1844 have a complete monopoly; and, under the privileges conferred by the Act upon the Bank of England, the monopoly is becoming every year intensified in its effects, because concentrated more and more in the hands of a single Bank, whose only rule of conduct is to charge the highest rate possible.—No wonder that the country suffers and complains.

XVI.

THE CURRENCY, PAST AND PRESENT

THE currency, as established by law in this country, has since 1844 become a veritable chaos. Let a merchant empty the contents of his purse, and there will be turned out, probably, some sovereigns, silver coins, and bank-notes. A sovereign is royal currency—coin of the realm; its weight and purity are guaranteed by the stamp of the Mint, and it is indefeasibly a legal tender in payments alike to the State and between man and man. The silver-pieces likewise are coins of the realm, but they are not a legal tender in payments above the amount of £2. Bank-notes are still more diverse in their character as currency. The notes of the Bank of England are legal tender, but not absolutely,—only so long as the Bank continues to give gold-coin in exchange for them on demand. The 210 other banks of issue in the kingdom have no such privilege; their notes are not a legal tender under any circumstances, however amply the convertibility of these notes may be

secured, and however perfect may be the credit of the banks which issue them.

Moreover, there are no less than three different bases upon which the note-circulation of the country is allowed to be issued; and the actual facts of the case may be summarised as follows:—(1.) The average actual circulation of the Bank of England (about 22 millions) is based, fully two-thirds upon Government securities, and rather less than one-third upon specie. (2.) The present note-issues of the Scotch banks are based one-half upon gold, and one-half (so far as legislation is concerned) simply upon the credit of these banks. (3.) The present note-circulation of the Irish banks is issued almost wholly upon their own credit,—that is to say, without the law compelling these banks to keep any special security for their issues. (4.) The notes of the 190 English provincial banks of issue are not based upon any special security at all; neither are they bound to pay specie for their notes on demand,—the notes of the Bank of England having been made legal tender, instead of coin, in payment alike of the notes of these banks and of their deposits.

Such is the chaos of currency which has been established in the United Kingdom by the existing monetary laws. Moreover, in addition to those startling anomalies, a vicious system of Monopoly, and an unworkable system of Restriction, have been superimposed; so that our whole banking-currency has become unintelligible in principle and retrograde in spirit.

When banking was first adopted in this country, by the establishment of the Bank of England and the Bank

of Scotland, very clear ideas prevailed as to banking-currency and the basis upon which it should be issued. The Bank of England was constituted as follows:—Firstly, it was a joint-stock company, consisting of a number of shareholders of good repute, both as regards wealth and character, each one of whom was liable to make good the obligations of the Bank to the full extent of his means. Secondly, the notes of the Bank were issued upon Government security,—*i. e.*, to the amount of the coin (£1,200,000) which the Company had lent to the State. The substantial value of the notes being thus secured, the State imposed no other condition on their issue. The Company was bound to pay coin of the realm (then chiefly silver) in exchange for its notes, when required to do so; but it was left to its own judgment as to the amount of coin which should be kept on hand to insure the convertibility of the notes. Thirdly, there was no compulsion laid on the public to receive the Bank's notes: the community was left free to accept them or not, as seemed to them best. The founders of the Bank knew that the notes of a sound establishment, enjoying the confidence of the public, require no "legal tender" character, no extraneous aid from the Government, to obtain circulation. (Even the Bank of France, at the present day, although the only bank of issue in that country, does not ask for *le cours forcé* for its notes.) Fourthly, when the Bank of England was established, no monopoly of any kind was granted to it: indeed, the principle of monopoly was expressly repudiated and condemned by its founder. Any company was free to establish itself as a bank of issue upon similar con-

ditions. To supply a safe and acceptable substitute for metallic money, and thereby to keep the currency adequate to the requirements of the community,—such was the object of the founders of the Bank of England, and such was the ground upon which Parliament proceeded at the establishment of the Bank.

The Bank of Scotland, established a year later than the English Bank—before the Union, and when the Scotch had a Parliament of their own,—was founded in the main on similar principles, but in a somewhat bolder and freer spirit. Like the Bank of England, it was a powerful joint-stock company, every member of which was liable in full for the debts of the bank; but no condition, no legal restriction, was imposed upon its issue of notes, save that they should be payable in coin on demand. Its notes were not a legal tender: if people did not wish to have the Bank's notes, they could refuse them at pleasure; if the public did want its notes, the Bank was at full liberty to supply them. Being secured by a large paid-up capital, and by an ample proprietary in reserve, the notes of the Bank of Scotland circulated as freely as those of the Bank of England. Also, no monopoly was either given or asked for. Banking in Scotland, as at the outset in England, was left free. Any company or firm was at liberty to establish a bank and issue banking-currency.

This system of freedom in Scotland bore noble fruits. One after another, at considerable intervals, as the monetary requirements of Scotland increased, large banks arose,—powerful companies, whose capital and proprietary furnished an ample guarantee for the notes which

they issued, and for the deposits which they received. This was a natural result of the system of perfect freedom. Left to themselves, the banks and the public settled the matter without difficulty or mistakes. Large banking-companies arose, because the public naturally preferred to deal with such establishments. Private banking was almost unknown, because it could offer no guarantee comparable to that of joint-stock banks. What is the credit of a single individual, compared to that of a numerous company, every one of whose members is liable to the full extent of his property? Under this perfectly free system of banking, not a single note-holder or depositor in Scotland has ever lost a shilling by the failure of any bank.*

While the free system was bearing such excellent fruits in Scotland, in England it was almost instantly supplanted by the opposite principle of monopoly. Banking in England speedily fell from the state in which it was created, and went to the bad. Within fourteen years of its establishment, the Bank of England used its powers and opportunities to obtain for itself special privileges. The Government was in want of money to carry on the war against the Grand Monarque,—the Bank agreed to raise the required amount of coin, and

* Moreover, the only case on record of the notes of any Scotch bank being in disrepute was for *one day*, in November 1857 (twelve years after the old Scotch system of freedom had been abolished by the Act of 1845), when the Western Bank stopped payment, and when the other Scotch banks—by a mistake which they afterwards acknowledged, and which they immediately rectified—momentarily hesitated to accept the notes of the suspended bank, although they knew that all the liabilities of that bank were amply secured by its large and wealthy body of shareholders.

lend it to the Government, on condition that no other joint-stock bank of issue should be allowed in England. The Government, pressed for money, assented; freedom in banking was summarily suppressed in England, and a monopoly was established on behalf of the Bank, which rendered the growth of a sound system of banks absolutely impossible. The prohibition against the establishment of any banking-firm consisting of more than six partners, was framed solely and avowedly to favour the Bank of England, in return for its loans to Government, by preventing the rise of any powerful bank which might compete with it. Thus, in return for getting a loan from the Bank, the Government of the day (A.D. 1708) inflicted upon the country a burden which, though little more than theoretical at the time, has since then repeatedly inflicted the most widespread disasters, and has done far more to checker the industrial career of this country than any other cause which can be named.

That happened which always happens. If you prevent a community from supplying their wants in the best form, they will do so—they are forced to do so—in an inferior way. Joint-stock banks being prohibited, a number of private ones arose. Great banks being wanted, but prohibited, their place was of necessity taken by small ones. Private gentlemen, merchants, even little shopkeepers, started as bankers in answer to the wants of their localities. In Scotland, the banks were established in the capital, or in one or two of the leading towns, from whence they extended their operations over the country by means of branches; so that a few great banks with numerous branches amply sufficed for the wants of

all Scotland. In England the case was quite otherwise. Private banks cannot spread over the country by means of branches. A private firm or individual may be well-known and fully trusted in his own locality, but his name and credit are not generally known elsewhere. It is only large banks, whose capital and proprietary are widely known, that can successfully extend their operations over the country; and in England no banks of this kind were allowed to be established. A vast number of petty banks was the natural, the inevitable result. Every little district or town had its little bank or banks, which, whether well-managed or not, had not that first requisite of a bank,—an adequate capital, as a reserve and guarantee for its operations.

These little banks, established in hundreds over England (at one time there was about a thousand of them), being possessed of small resources, fell in scores on every occasion of panic or crisis. It was not their note-circulation which brought them down, or which brings down any bank: in all cases the chief and primary cause of their fall was a run for deposits,—a sudden calling-up of the money intrusted to them. In fact, when a bank's credit is shaken, it is always the depositors who are the first to take alarm, and whose demands, being largest, it is most difficult to meet. Few persons have more than £10 in notes on hand: hence note-holders are never so prompt and eager to make a run upon a bank as the depositors are, who have hundreds or thousands at stake. Having no large paid-up capital or reserves, those English banks, whenever a crisis of any kind occurred, gave way in scores, spreading loss and ruin over the country.

Ever and anon, a number of those weak banks lost credit,—their notes, forming the chief part of the provincial currency, became useless, and the depositors in those banks lost still more heavily than the note-holders.

These repeated failures of the English banking-system necessarily excited great attention. The evil was too momentous to be overlooked. But the Government did not discern the real cause and root of the evil. They failed to see the simple truth, that it is impossible to have a sound banking-currency without sound banks. And a sound system of banks could not be established, owing to the monopoly conferred upon the Bank of England. The Government allowed the root of the evil to remain, and meddled and muddled with the note-issues. Like an ignorant physician who has to deal with an eruptive complaint, they attempted to cure the disease by putting a plaster on some of the eruptive spots. They prohibited the further issue of small notes: which small notes seemed to them to be the great cause of the malady. It never occurred to them to consider how it was that small notes, which formed a large portion of the banking-currency of Scotland and Ireland, had not only produced no catastrophe in those portions of the kingdom, but had proved eminently beneficial. Small notes—that was the only thing which the Government could imagine as the root of the evil: and accordingly small notes were abolished in England.

The evil, of course, was not cured: and in a few years afterwards (1833), the Government again attempted to improve the state of matters, by making the notes of the Bank of England a legal tender. As a cure for

the frail condition of the English banks of issue, they increased the system of monopoly which was the primal and fundamental cause of the unsoundness of the general banking-currency of England. Still the system remained unsound, in the estimation of the very statesmen who had so long been promulgating remedies, or at least prescriptions for it. But again the seat of the malady was not perceived. Perplexed by the failure of all the former prescriptions, Sir Robert Peel, in 1844, prohibited the further extension of banking-currency altogether; at the same time purchasing the assent of the existing banks of issue to this measure by conferring upon them, throughout the whole kingdom, a monopoly of the note-circulation. No additional notes were allowed to be issued by the banks established prior to 1844;* and no new bank was allowed to issue banking-currency at all.

This measure was the more to be regretted inasmuch as, for some years previous, an element of improvement had been introduced into the English banking-system, which, if allowed freely to develop itself, would ere long have gone far to remedy the weakness of the English note-currency. This was the establishment of joint-stock banks. In 1826, joint-stock banks of issue were allowed to be established in the provinces (beyond a radius of

* This is the literal fact as regards all the English banks of issue, except the Bank of England. And although the Bank of England and the existing banks of issue in Scotland and Ireland were allowed to extend their note-issues, it was only upon condition of keeping an equal amount of gold in reserve — a condition which nullified the economy which is the object of banking-currency, and which left the banks but little motive for issuing it.

sixty miles from London); and, in 1833, joint-stock banks, *but without the power of issuing banking-currency,* were allowed to be established in London itself. This great strengthening of the basis of banking in England also afforded a means of improving the banking-currency of England. But Sir Robert Peel overlooked this circumstance. Wearied and bewildered by the inadequate results of previous legislation on the subject, in which he had taken a chief part, he came to regard banking-currency as an evil altogether,—a necessary evil, he was forced to admit, but one which, as it seemed to him, it was expedient to reduce to the smallest possible proportions. Hence the restrictions which he imposed upon the right to issue banking-currency. Moreover, seeing that the Bank of England was the only great bank of issue in England, and possessed the greatest security for its note-circulation (forgetting that it was so only in consequence of its long-established monopoly of joint-stock banking), he resolved, so far as was practicable, gradually to suppress all the other banks of issue, and give to the Bank of England an absolute monopoly of the banking-currency of the country. And yet, strange to say, he took no measures to prevent the abuse of so vast a monopoly. He left the Bank, as it was, a private establishment, whose chief object is to increase the profits of its shareholders; yet he also left it free to charge what it pleased for the use of its notes! He established for the Bank a virtual monopoly of the English banking-currency, without considering what would be the effects of such a monopoly upon the interests of the community.

Thus the banking-system of this country, as established by Act of Parliament, exhibits four features which specially challenge attention. (1) The banking-currency is fixed in amount: unlike that of other countries, it is no longer allowed to expand with the growing requirements of the community. (2) It is subject to a monopoly; without any safeguard against the abuse of that monopoly. (3) The conditions of its issue are wholly anomalous. (4) A portion of the present bank-issues is inadequately secured.

There are four different and incongruous laws for the banking-system of this country. There is one law for the Bank of England, another for the Scotch and Irish banks, a third for English provincial banks of issue, and a fourth for all banks established since 1844. These diversities of legislative enactment are not justified by any corresponding diversity in the constitution and circumstances of the banks to which they apply. We do not object to them merely as diversities, but because some of them are bad. For example: it is a most objectionable thing that there should be scores of private firms, some of them consisting merely of single individuals, allowed to issue banking-currency in England, while there are many powerful joint-stock companies, notably those of the metropolis, which are not permitted to issue banking-currency upon any terms. Moreover, the enactment which regulates the provincial banking-currency of England is inadequate. There are two ways of securing the solidity of banking-currency: namely, either by taking direct security for the notes issued, or by insuring that they shall only be issued by

banking-companies of large resources. In neither of these respects is any security taken for the provincial banking-currency of England. It is only justice to say, that since 1844 the English provincial banks of issue have on the whole been well conducted; and that, as a matter of fact, there is no ground of complaint against them. Nevertheless, we cannot regard this portion of our banking-currency as adequately secured.

Finally, our whole banking-system is subjected to the monster evils of Restriction and Monopoly; the consequences of which every year weigh more heavily upon the community. First, as to Restriction. Banking-currency is simply the exchange of one kind of property for another. It is an exchange of one kind of negotiable property into another kind which is more widely negotiable. That is all. It is a conversion of commercial currency and other readily negotiable securities into general currency. Hence, on principle, to fix the amount of banking-currency in a country is as absurd and indefensible as to fix the amount of commercial currency. More trade requires more currency. Commerce does its part by providing a currency of its own. But what happens when there are no adequate means of converting this currency of trade into general currency? Ever-recurring grievous disasters alike to trade and to the community at large. Banking-currency, and with it the whole currency, tends to rise in value; and ever and anon the measure of value in this country is altered to such an extent as to produce most serious disasters. During the last dozen years, the average charge for banking-currency (*i. e.*, the bank-rate) has

been increased 50 per cent. And the temporary fluctuations are far more serious. Ever and anon the bank-rate is raised upwards of 100 per cent above its ordinary level; and, as a natural consequence, prices in the great produce-markets fall 20 or 30 per cent.

Secondly, as to Monopoly. Even if the amount of banking-currency be not fixed (by unwise legislation), the supply of it will not be regulated by the natural law of supply and demand if the right to issue it be a monopoly, possessed by a certain bank or banks, upon whom no check is imposed to prevent an abuse of their privileges. The banks of France and Belgium have a monopoly of the banking-currency of those countries; but in both of these cases the State, while conferring a monopoly, has imposed a check upon the abuse of that monopoly. These banks may raise the rate of discount to any point they like, but they are not allowed to profit by any increase in their charges beyond the limit of 6 per cent. If these banks think it necessary for their security to raise the rate to 7, 8, or 10 per cent, they may do so: but they can gain no more profit than if they charged 6 per cent. *They are not permitted to convert their difficulties into a means of increasing their profits.* If a monopoly of banking-currency is to be established at all, this is the right way to proceed. In this country, on the other hand, the supply of banking-currency, instead of being left free (as in all other countries) to expand with the growing wants of the community, is restricted to a certain amount; and at the same time the right to issue it is a monopoly, against the abuse of which no precautions of any kind have been taken.

Such a system is alike false in principle, and most injurious in practice. When, during the crisis of 1866, the Bank of England obstinately maintained the bank-rate, the minimum charge for its loans and discounts, at 10 per cent, the other great banks in London openly protested against this exorbitant charge,—not only as excessive, but as tending to perpetuate the crisis and aggravate the national disaster. In this view they were supported by the *Times* and the *Economist*, and the result has shown that they were right. But those great banks were practically powerless. They are not allowed to issue banking-currency. They have to conduct their business with notes of the Bank of England. And so the Bank went on its own way: most profitably to itself, however disastrous its procedure was to the community,—to the interests of trade and industry, to the general wealth of the country, and to the employment of the toiling myriads of our population.

The object for which Banking was established in this country was twofold:—To convert commercial currency and other suitable securities into general currency, in accordance with the requirements of the community; also, and chiefly, to issue banking-currency as a substitute for metallic currency, the supply of which had even then become inadequate for the ever-growing wants of the country. Banking in this country—as afterwards in France, America, and most other countries—was established primarily, we might say solely, for the purpose of issuing banking-currency, or notes convertible into specie on demand. Deposit-banking was almost unknown. It was as banks of issue that

the Bank of England and the Bank of Scotland were established: banks of issue for the discount of bills and the making of loans, thereby supplying the community with currency in proportion to its requirements. Such, also, was the object for which the Bank of France was established; and so subordinate even yet is its deposit-business, that that great and most successful establishment is little else than a grand bank of issue, supplying the community with currency in accordance with their varying requirements, through its loan and discount business—*i.e.*, in exchange for bills and other readily negotiable securities.

Yet nowadays, in this country, banks are regarded as if they had no business to issue promissory notes at all. Every other branch of trade is allowed to utilise its credit in this way. Notes are to banks what bills are to the rest of the community. What would be thought if the Government were to confer a monopoly of the right to issue bills upon a dozen commercial firms, and were to prohibit all the others from doing so? The result would be that the privileged firms would make use of their monopoly as a means of increasing their gains, howsoever disastrous the results of such conduct might be to the community —to the interests of Trade and the rights of Labour.

Free-trade is a good thing: but in order to be fully effective, the principle must be applied to that trade of trades—to the trade upon which all others depend,—namely, Banking. At present, Free-trade, even in its purely Commercial aspect, is robbed of its due development by the opposite principle of Monopoly and Protection which vitiates our Monetary system.

XVII.

FOREIGN SYSTEMS OF BANKING

THE monetary system of the United Kingdom is alike anomalous in itself, and dissimilar from that of any other country, either at present or in any former time. Before considering how our monetary system may be improved, and brought into harmony alike with the spirit of the age and the interests of trade and industry, it may be instructive, as a prelude, to exhibit briefly the various modes in which banking, and especially the issue of banking-currency, is carried on in other countries than our own:—

FRANCE.

In France the issue of bank-notes is a monopoly, checked by the same law which establishes it. The Bank of France may issue as many notes as it finds expedient, but it is not allowed to make a profit upon such issues above a certain rate. It may raise its charge (the

Bank-rate) to any height it may think necessary for its safety, but it is not allowed to reap any profits upon its note-issues above 6 per cent. This legal enactment nullifies the cardinal fault of a monopoly, by taking from the Bank all motive for raising the rate for the mere sake of adding to its profits. All profits above 6 per cent are, for the present, added to the capital of the Bank of France; so that, although they may slightly enhance the price of the Bank's shares, they are not divisible among the shareholders. But this is merely a provisional arrangement; for as soon as the capital of the Bank is considered large enough, the profits above 6 per cent on the issue of notes will thereafter go to the State.

Thus the worst feature of a monopoly is avoided. Nevertheless, the prohibition to issue notes works badly in one respect—namely, it prevents Banking being carried promptly into the country districts and small towns, where *mere deposit-banking* will not pay (at least at the outset), but where (judging from the experience of our own country) banks would be readily established, if they were allowed to issue notes.

*"The Bank of France, although possessed of a monopoly, is not a purely private establishment, like the Bank of England, whose only object is to obtain the largest dividends for its shareholders. Practically the Bank of France is kept in check by legislative enactment, and holds itself amenable to public opinion, and to the interests of the State. Nevertheless, the system of mono-

* The following paragraphs in regard to the Banking system in France are extracted from my Deposition to the French Government's Inquiry into Banking and Currency in March 1866.

poly, which is so rigidly established in French banking, is bad—bad not merely theoretically, but bad in its practical everyday working. The system is not favourable to the progress and development of the country; and every year the system will become less adequate. Even if progress were not the law of the world—even if France were to stand still in other respects—it would be advisable to alter her Banking-system. But France will not stand still. She will progress in the future as she has done in the past. And with a view to this, it would be well to introduce, at once and without delay, a free system of banking. The note-circulation of the Bank of France has trebled during the last sixteen years; what, then, will be its magnitude by the end of the century? Doubtless the cheque-system will ere long be adopted extensively, and will lessen the rate at which the note-circulation is at present increasing. But still, independently altogether of the note-issues, if the present monopoly be maintained, the magnitude of the Bank will be monstrous, overpowering, before the present generation has passed away.

"It were wise, then, to begin at once a system of free banking in France. But in the case of the new banks of issue, they should be required to deposit with the State, as security for their notes, an equal amount of Government stock. Such a security would give confidence to the community, and would thereby help to develop the system. At the same time, such a system would leave the Bank of France unshorn of its present prestige and power. It would mitigate the overgrowth of that establishment, which otherwise must ensue in

the future; but it would still leave quite as much centralisation in the Banking-system as even Frenchmen can desire. The Bank of France has got a long start, and will keep it; but (to borrow a simile from the race-course) she will go differently and better when she finds she has not got all the running to herself.

"As long as the monopoly of the Bank of France continues, not merely legally but practically—that is to say, until the new banks collectively are able to enter into effective competition with it—the qualified maximum at present imposed upon the Bank's rate of discount ought unquestionably to be maintained. The present law imposes no restriction upon the Bank-rate; the Bank is perfectly free to charge any rate which may be necessary or expedient to protect its interests; but above 6 per cent the profits are not to go into the pockets of the shareholders. But for this enactment, the Bank (like all other privileged banks) would seek to raise the rate exorbitantly, not as a precautionary measure, but simply as a means of adding to its profits. The difficulty to which a bank is subjected when its stock of specie is diminished is, that it is less able than usual to meet its liability to pay its depositors in specie; and it is a novel idea (comparatively recently adopted) that banks should convert this difficulty into a means of increasing their profits. Under a regime of freedom of issues, the State should not interfere, and the rate of discount should be settled by the natural competition among the banks themselves. But the case is quite different under a regime of monopoly. The Government which confers the monopoly is bound to take precautions against the

abuse of that monopoly. Every privileged bank makes excuses by the dozen—it affects apprehensions of all kinds in order to justify it in charging exorbitant rates. At the same time such privileged banks—notably the Bank of England—take no steps to provide themselves with specie. They simply make their difficulties, which they do not stir a finger to obviate, a means of adding largely to their gains at the expense of the community. Every bank is eager to raise the rate of discount: at the same time not one of them, if it can avoid doing so, will incur the cost of providing itself with specie when more specie is required. The only remedy for these evils is, to subject the privileged bank to an effective competition. And until the new banks are established, and their competition becomes effective (which is not likely to be soon), the qualified maximum imposed upon the Bank of France ought to be maintained.

"Banking in France is still very much circumscribed in its sphere of operations. It requires to be extended into all parts of the country. And the new banks of issue which I have proposed would give a great impulse to this extension. At present there are hundreds of little towns where it would not pay to establish a bank merely of deposit. In such places a large amount of spare money and small savings lies idle in the hands of shopkeepers, farmers, and others: it is just so much reserve-wealth withheld from the general store—from the reservoir which sets in motion the thousand wheels of the national industry. But as soon as banking is introduced into those localities, the spare money, the small hoards of the district, are economised: they are concentrated

in bank, and thereafter sent to where they are wanted—to the great centres of trade—to the money market. It may be said that all this may be done without the help of new banks—by the Bank of France itself. The Bank may establish branches in every little town or village in France. So it may; but it will not. It is not worth its while to do so. If banking is to be introduced into those comparatively poor localities, it must be accomplished by some other agency than that of the Bank of France."

It may be added that, except the Bank of France, there are no banks in France, in our sense of the word, —the *Banquiers*, of whom there are several hundreds, being equivalent to our bill-discounters.

BELGIUM.

In Belgium the banking-system is regulated on the same principle as in France. It is a regulated monopoly. There is only one Bank of Issue; and, as in France, the privileged bank is kept in check by legislative enactment. The only difference is, that in Belgium the profits on the Bank's issues above 6 per cent go directly to the State. I may add that, as Belgium is a very small country, easily reached in all parts by the Central Bank, the evils of a regulated monopoly are even less than in France. In fact, practically, there are no evils to complain of at all.

HAMBURG.

The Bank of Hamburg, one of the oldest in Europe, is simply a bank of deposit. It has never been allowed to issue notes. But this fact is not only no safeguard against monetary crises, but, as shown in 1857, it tends greatly to intensify such a calamity. The Bank's credit on that occasion was perfect, but the Bank could not supply Currency, which at that time was in unusual demand. In this emergency the Municipality (or State) issued State Bonds; but these, being for large sums, and therefore not available as general currency, had to be taken to the Bank or to private capitalists for discount—*i.e.*, to be exchanged into general currency: and the demand for money was so great that the banks had not the means of doing this. At last the Municipality resolved to import a large amount of silver (the only currency recognised in Hamburg), by getting a loan from Austria; and the moment the first instalment of this supply of Currency arrived, the Panic was at an end.*

The Bank of Hamburg is the only existing case that can be given (so far as I know) of a Bank purely of Deposit, and without the use of Paper-money.

THE UNITED STATES.

The old system of banking (not yet entirely displaced) in the United States was, that any bank might issue

* For further details, see Appendix to my *Economy of Capital*, pp. 442-443.

notes, on the deposit of an equal amount of the bonds or securities of the particular State in which it was established. The new system of the "National Banks" is based on a similar principle,—the difference being this, that instead of local State-bonds, the banks must deposit bonds of the Central or National Government; and upon these they are allowed to issue notes to nine-tenths of the amount.

At present, owing to the recent exigencies of the State, convertibility of the notes into specie is not required. The bank-notes are convertible only into Government notes (greenbacks). But this is regarded as a temporary arrangement; and ere long the National Banks, like the old banks, will be bound to convert their notes into coin on demand.

Within my own memory and observation, especially during the crisis of 1857 (every phase of which I observed most carefully), the old system of banking in the United States worked exceedingly well. In 1857, owing to the panic-run for specie in payment of deposits, all the banks of the New England States, New York, and Pennsylvania, suspended payment: but, *even then*, their notes were not depreciated—they circulated at par with coin as before. Indeed, by a singular conjuncture of circumstances, it is a fact that at one time during the suspension the notes of those banks were actually at a premium compared with gold.*

As regards the New System, some of its provisions are inadequate to attain a proper security for safe bank-

* See extract from City articles of the *Times*, quoted in *Economy of Capital*, p. 294, 295.

ing, and would be quite inadmissible in this country: nevertheless, in a new country like America, with its vast undeveloped resources, it is considered that the risks of the new system are more than counterbalanced by the impetus which it imparts to material progress and productive industry.

At present, when there is a movement in this country in favour of the State taking the right of issue into its own hands, it is important to observe the course taken in this matter in the United States. By the issue of greenbacks the Government had actually flooded the country with State-notes. Therefore all that the Government had to do, if it wished to adopt the principle of a State-issue, was to declare that the banks were to deal with those notes exclusively, and to issue none of their own. But the American Government has done, and continues to do, exactly the reverse. It was compelled by circumstances to issue notes of its own—*inconvertible*, as all State-notes are, or tend to become: but its desire is to withdraw these State-notes altogether, and to allow the entire note-issues of the country to be supplied by the banks.

The Banking-systems thus briefly described are typical. They exemplify the system of Monopoly of Issue in its best form, as in France and Belgium; of Free-trade in Banking (somewhat recklessly applied), as in America; and lastly, the obsolete system of mere Deposit-banking and metallic currency, as in the case of the Bank of Hamburg.

Of these three systems, that of the Bank of Hamburg

is totally inadmissible in this or indeed any other progressive country: it is as much a relic of the past as is the skeleton of a mammoth or a mastodon. The system of the Bank of France—though really superior in practical working to our present monetary system—is not likely to be adopted in this country, owing to the magnitude of the monopoly which it involves. The only alternative, then, seems to lie between the adoption of a free system of Bank-issues, guaranteed by a deposit of Government securities,—and the creation of a system of convertible State-issues, for which there as yet has been no precedent, but which nevertheless is deserving of consideration.

XVIII.

THE STATE AND THE CURRENCY

THERE is much that is alluring in the proposal that the State should take into its own hands the issue of our paper-money. It seems so simple; it also, at first sight, seems so profitable for the State. If banks make a profit on their note-issues, why should not the State be able to do the same? And if the State can make such a profit, why should it not do so? We need hardly remark that proverbially the State is a bad man of business; that trade is alien to its functions; and that many a business which is profitable in private hands, becomes unprofitable in the hands of a Government. Still less need we observe, as a question of principle, that the less a State interferes with industry the better; and that the best thing for a Government is to mind its own business—namely, governing—and to leave the community to mind theirs. Instead of dealing with those wider views of the matter, let us look at the more practical points of the case.

The first point to be noted, in considering the proposal for a State-issue of paper-money, is the experience of the practical working of such a system in cases where it has been already tried. Our own country furnishes no examples of this kind, but they are plentiful enough in the history of other countries. From the days of the Venetian Republic—not to go back to Rome during its critical war with Carthage—down to the present hour, the system of a State-issue of paper-money has been repeatedly and extensively adopted. But in all those cases it has been an exceptional measure,—always exceptional in its causes, and generally brief in its duration. It has never been long maintained except in countries like Russia and Austria, where the indebtedness of the State—or, in other words, a deficit of the revenue compared with the expenditure—is a chronic condition of affairs. In the War of American Independence against this country, the belligerent States issued paper-currency as the only means by which they could sustain the conflict. A few years afterwards the same system was adopted by France during her Revolution —in the form of Assignats, or paper-money issued on the security of the old Crown lands. In both of these cases the notes thus issued became rapidly so depreciated as almost to be worthless. In 1796, assignats of the nominal value of £40 barely sufficed to pay for a five-shilling dinner. The depreciation of the American State-notes was equally great. Since then various Governments of Europe have had recourse to an issue of State-notes, in every case from the same causes, and with a more or less similar result. During the recent

civil war in the United States both the Federal and the Confederate Governments had recourse to the same system; the result being that, in the case of the Southern States, the State-notes became almost worthless; and in the case of the successful Northern States, the notes became depreciated during the conflict 150 per cent, and even now they are still 30 per cent below par. A hundred dollars in specie are equal in value to 130 dollars in greenbacks. In fact, in every instance of which we have as yet had experience, a State-issue of notes has been simply a forced loan in disguise: just as it was (to take the most recent instance) in Italy during the war with Austria in 1866. Hitherto the system has never been adopted by any Government save as a means of meeting an inexorable necessity—as a means of tiding over a grand national emergency. It has been adopted simply as a means of enabling the Government to expend more money than it received, or could obtain by any means, from the community. A deficit of revenue, compared to expenditure, has not hitherto been regarded by any Government as a sufficient reason for adopting a State-issue of notes: as long as a Government could obtain a loan, either from its own subjects or from other countries, it has abstained from having recourse to this extreme measure. It is only when taxation has been pushed to an extreme, and when even loans are unprocurable, that Governments have adopted the system of issuing State-notes; and as a natural consequence, they have at the same time found it necessary to give a forced circulation to those notes, by making them a legal tender, not only in payments

to itself in the form of loans and taxes, but also as between man and man.

These facts cannot be put out of sight. Every issue of State-notes either is from the outset depreciated, compared with the value in specie which they purport to represent, or it tends to become so. Of course this does not settle the question. Although State-notes have become rapidly, and in most cases enormously depreciated, in every instance in which they have been adopted in other countries, it does not follow that a like result would follow the adoption of such a system in our own country. It may be argued that if our Government, even during the exigencies of the terrible war with Napoleon I., never had recourse to an issue of State-notes, it is in the highest degree improbable that, if such a system were normally established, our Government would ever so use its power of issuing paper-money as to lead to a depreciation of the currency. Nevertheless, if there had been an established system of State-notes in 1797—if the Government had then possessed the power to issue notes of its own—we think it would not have hesitated to use those notes in partial payment of its expenditure. It is one thing for a Government to ask power to issue notes of its own, it is a very much easier thing to apply or misapply that power when already conferred upon it.

It may be said—The Government in 1797 authorised the banks of the country to suspend cash-payments: how would things have been worse if it had issued inconvertible notes of its own? We reply, the difference would have been immense. The two operations are

totally dissimilar. In both cases, it is true, the safeguard against over-issues and depreciation of the currency which "convertibility" supplies would be temporarily removed; but the tendency to over-issue in the two cases would not be alike. An issue of State-notes is regulated not by the monetary requirements of the community, but by the exigencies of the Government. The Government expenditure in such a case is made in inconvertible notes, and there is no efficient or self-acting check upon such issues, so that they may be continued until a great depreciation of the currency ensues.

On the other hand, a temporarily inconvertible banking-currency is not, or at least is much less, prone to over-issue and depreciation. And for these reasons: 1. Banking-currency of any kind can only be issued in answer to the demands of the community. It can only be issued in the form of discounts and loans upon which the bank-rate is charged, and no man will pay interest for money which he does not need. 2. The only way in which banks can in this way get out a larger issue of notes than usual is by reducing the rate of discount—thereby inducing the community to apply for more discounts and advances than it would otherwise do. But no bank is willing to reduce the profit on its business, and it is always most profitable for a bank to keep its charge at the highest possible amount. For example, say that a bank has a discount-business of ten millions, and charges thereon 5 per cent: if it reduces its charge even 1 per cent, it will require to increase the amount of its discount-business 25 per cent before it can recover its former amount of profits. Hence, even when tem-

porarily exempted from the duty of paying their notes in specie, banks have no motive for increasing their issues beyond the natural requirements of the public: that is to say, they have no motive for making the currency redundant and depreciated, seeing that this can only be done by an undue reduction of the bank-rate, or, in other words, of the amount of their own profits.

The idea of a State Bank of Issue probably floated dimly and vaguely, as an object of the future, before the late Sir R. Peel when he framed the Acts of 1844-5; and of late years it has frequently been proposed in a crude form, in pamphlets, without any definite plan for the practical working of such an establishment. A year ago, in the debate occasioned by the great crisis of May 1866, Mr Gladstone seems to have adopted the idea, as a remedy for the existing defects of our present monetary system. He said briefly, but emphatically—"The profit of issues [banking issues or notes] belongs to the State; and what is much more important than the profit, the responsibility of issues also belongs to the State." Here, then, we have two distinct propositions: let us consider them in succession.

In making these statements, Mr Gladstone offered no proofs or arguments in their support. And it must be admitted, as regards his first proposition—namely, that the profit on bank-notes should belong to the State—that, *primâ facie*, the conclusion is quite the other way. In the first place, as a matter of fact, there is no country in the world in which, either at present or at any time, it has been held that the profit on banking-currency belongs to the State. And secondly, as a matter of

opinion, one would naturally think that the profit on the issue of such promissory notes should belong to the establishments which issue them at their own risk, and which have to keep a stock of gold requisite to insure the convertibility of those notes.

Bank-notes are a kind of general currency which banks issue in exchange for commercial currency (bills) and other property of a readily negotiable character. And banks must have a profit on this kind of business, otherwise they will not carry it on. They have first to get a return for their paid-up capital, or such portion of it as is needed as a guarantee for the notes which they issue. Secondly, they keep up a special department for the issue of notes,—which of course costs money. Thirdly, they have to incur the risk of some of the securities, in exchange for which they issue their notes, proving bad,—in which case they must bear the loss. And lastly, they must at all times keep in hand a stock of gold (which yields no interest) to give in exchange for their notes on demand. In these various ways, the issue of notes entails risk, and moreover constitutes a pretty heavy expense to banks. It is easy to see, then, why the profits on banking-currency should go to the banks which issue it,—as is, and ever has been, the custom in every country where banking-currency exists; and accordingly the onus of proving the correctness of the opposite opinion—namely, that "the profit of note-issues should belong to the State"—lies entirely with those who advance it.

The matter resolves itself into (1) an abstract question of right, and (2) a practical question of public

advantage, or *cui bono?* As regards the question of right, the leading principle may be safely laid down. The State may impose a tax on bank-notes on the same principle on which all other taxes are imposed,—namely, as a means of raising revenue from classes or persons who otherwise would not bear their fair share of the public burdens. Bank-notes may be taxed just as bank-cheques and commercial bills are taxed, or as any other media of transferring wealth are taxed. But not otherwise. The State has no more right at present to the profit upon bank-notes than it has to the profit upon commercial bills. In truth, it has no more right to appropriate the profit upon the issue of banking-currency than it has to appropriate the profit upon any other kind of business which it does not itself carry on.

It may be said that the State has a right to levy a seigneurage upon the legal money of the realm. But this argument is partly invalidated by the practice of this country; and what is more, it is quite inapplicable to the present question. 1. As a matter of fact, such a system has been repudiated in this and most other countries. In England, the State does not only levy no seigneurage upon the coinage, but it does not even charge for the cost which it incurs in coining. A costly establishment is kept up for the purpose of doing all the coining gratis. Any person may take any amount of gold to the Mint, and he will get it turned into coin of the realm free of charge—*i. e.*, at the expense of the State. 2. Moreover, to levy a seigneurage upon money is justifiable only when the State agrees to receive that money at all times and indefeasibly in payment of taxes,

&c.; and also when, by making that money a legal tender under all circumstances, it enforces its acceptance upon the community at large. It is needless to say that the State does not do this in the case of bank-notes. Although there are fully 200 banks of issue in the kingdom, there is only one of those banks whose notes are in any degree a legal tender; and even in this case (that of the Bank of England) the "legal tender" character of the notes, besides being restricted to England, is not indefeasible,—the notes being liable to become worthless, like those of other banks, the moment the Bank of England fails to convert them into gold on demand.

Next, let us consider the practical question: What benefit would accrue to the community if the State were to appropriate to itself the profit upon the issue of bank-notes? If such a change were made, what good would it do? Or would it do any good at all?

Every tax imposed upon the banks is a burden which they at once shift on to the shoulders of their customers —in other words, the community. If the State were to levy a million a-year from the banks, there would and could be no gain; for the community would have to pay the amount in additional charges for banking-accommodation. Moreover—and this is the important point—this burden, when so shifted, becomes vastly augmented. As with a hydraulic press, an ounce of weight placed upon the small end is transmuted into a hundredfold pressure upon the broad end; so is every burden laid upon banks converted into a vastly greater burden upon the community. The increased charge exacted from the

public may simply compensate the banks for the State-tax imposed upon them; but this recouping necessarily takes place in such a way as enormously to aggravate the burden when so transferred to the shoulders of the community. The banks raise their charges in various ways; partly by paying less interest on deposits, and partly by declining to keep their customers' accounts on the same terms as before; but chiefly by raising the bank-rate,—*i. e.*, the charge which they make upon their discounts and loans. Now, what is the effect of such a rise of the bank-rate? When the rate of discount is raised to a high point, the effect is, not only to give to the banks a proportionately larger share of the profits of trade and industry of all kinds, but also to depress prices: so that a trader has not only to pay much more for his customary banking-accommodation (*i. e.*, for the discount of the bills by which trade is carried on), but his produce or stock of goods is simultaneously depreciated by the fall of prices which in such cases takes place. Thus, to take an extreme case, say that the bank-rate is raised from 5 to 10 per cent: then, although the banks receive only 5 per cent more on their transactions, although they take only (if we can say "only" in such a case) 5 per cent more of the profits of trade, the commercial classes lose, in addition, 20 or 30 per cent on the sale of their goods, owing to the concomitant depression of the markets. Moreover, when the bank-rate is raised to this high point, bills (the ordinary currency of wholesale trade) fall into disrepute, because commercial credit is shaken by the fall of prices; so that the bills of many traders are no longer accepted in pay-

ment; and, in consequence, many of those firms (although essentially solvent), being deprived of the ordinary means of carrying on their business, are forced to suspend.

Thus the effect of a rise of the bank-rate from 5 to 10 per cent is not merely an appropriation by the banks of 5 per cent more than usual of the profits of trade: it entails simultaneously upon the trading and producing classes a further loss of 20 or 30 per cent on the sale of their goods; and also by bringing the ordinary currency of trade (*i. e.*, bills) into disrepute, it deprives many firms of the means of carrying on business, and forces them into the *Gazette*. This is the effect of a high bank-rate upon the commercial and manufacturing classes; and upon the lower classes the effect is equally disastrous. The contraction of trade occasioned by a high bank-rate throws a large portion of the working classes out of employment,—entailing unmerited suffering upon thousands of industrious families, and also adding heavily to the poor-rates. Banks at such times get 5 per cent more than usual upon their discounts and advances; but, in consequence, a large portion of the trading-classes lose 25 or 30 per cent. Trade collapses, poor-rates increase, the national prosperity is checked, and all this is accompanied by a great amount of individual suffering and distress, alike in the middle and the lower classes.

Although the above is an extreme case, it correctly describes the effects of a rise in the bank-rate: and it is by a rise of the bank-rate, chiefly, that banks must seek to compensate themselves for any heavy tax imposed

upon them by the State. Indeed, it is no exaggeration to say that for every gain made in this way by the State, it would be better for the community to pay twenty times as much in the shape of ordinary taxation. Hence, if a heavy State-tax upon the note-issues of banks be a positive detriment to the community, the actual appropriation by the State of all the profit on such bank-issues would obviously be still more detrimental.

But although it be neither justifiable as a question of right, nor advantageous for the common weal, that the State should appropriate the profit upon the present issue of currency by the banks, it is perfectly justifiable for the State to take such issues into its own hands; or, to speak correctly, to cause the present note-circulation of the banks to be withdrawn, and to replace it by a State-issue of paper-money, convertible, like the present bank-notes, into specie on demand. And this, we may presume, is what Mr Gladstone had in view when he made his remarkable statement last year—namely, that "the profit of note-issues belongs to the State; and what is much more important than the profit, the responsibility of such issues also belongs to the State." The first clause of the sentence is obviously untenable of itself; but, liberally construed, the meaning of the whole statement may be taken to be, that the State itself ought to become the fountain of paper-currency,—assuming the cost and responsibility of the issue of notes, and thereby entitling itself to the profit that may accrue from such issues.

This is a proposal quite intelligible in itself, and also

perfectly justifiable in principle. The only question, and a most important one, to which it fairly gives rise is: How would such a system work? What would be its practical effects? And would those effects be advantageous to the community?

The object of the proposed change, it is almost needless to say, is simply to place the paper-currency or note-circulation of the country on an improved footing, with the double view of increasing its validity, and of freeing its issue from the invidious influences of private interest which at present affect it. We shall endeavour briefly and clearly to exhibit the advantages of such a system, as well as the objections which may be taken to it.

Apart from the anomalous system which at present exists in this country, the defects of which we have shown in a previous chapter,* there are three distinct forms in which a paper-currency can be established. 1. By a plurality of banks, all equal in the eye of the law, and conducting their operations (like all other trades) on the principle of freedom and competition. 2. By a single bank of issue, upon which the State has conferred a monopoly,—subject to certain conditions, which ought to be designed not only to secure the convertibility of the notes, but also to prevent the abuse of the special privilege conferred upon the Bank. 3. As issued directly by the State,—the State taking upon itself the cost and responsibility connected with the business, and also acquiring any profits which may arise from it.

In deciding which of these systems is the best, there

* See Chapters XIV., XV., and XVI.

are two main points to be kept in view. Firstly, the Validity of the Note: that is to say, the constant acceptibility of the paper-money of the country as a valid tender in payments and all transfers of wealth. Secondly, the Steadiness in Value of the currency—the measure of value, in which all contracts are made, and by which trade of all kinds is carried on; so that when a man engages to pay a certain sum of money, that sum, when the time of payment arrives, shall possess neither more nor less value (as measured by the amount of property or labour which it can purchase) than it possessed at the time when the contract was made. A perfect system of currency ought to attain both of these objects fully. And the best system is that which attains both in the greatest degree.

But as is obvious, these two requisites of a perfect currency-system do not necessarily go hand-in-hand. Each rests upon a separate basis. A currency may be made a valid tender, yet be subject to great fluctuations in value. "Validity" may be secured either naturally, by the convertibility of the notes into specie on demand; or artificially, by the State rendering acceptance of the notes compulsory upon the community. But neither of these methods constitutes any security for Steadiness of Value in the currency: for, in the first case, the value of the currency may be greatly raised at times when an export of specie takes place, or when from any cause specie is in greater demand than usual; and, in the second case, the value of the currency may be greatly depreciated by an over-issue of notes, although the notes remain a legal tender as before. In neither case is there

any security that the notes shall constantly possess the same purchasing power. In order to keep steady the measure of value (*i.e.*, the purchasing power of the currency) two points must be attended to. 1. The currency must not be liable to increase while the monetary requirements of the community remain stationary, otherwise the value of the currency will be diminished. 2. The amount of the currency must not remain stationary when the monetary requirements of the community are from any cause increased, otherwise the value of the currency will be raised. In order to insure steadiness of the measure of value, the amount of the currency and the monetary requirements of the community must always be commensurate, the currency increasing or diminishing in quantity in accordance with the natural law of supply and demand.

Let us apply those tests to the three systems of issuing paper-currency above-mentioned.

Firstly, as regards the question between Plurality of Issue and a Single Bank of Issue:—Plurality of Issue —that is to say, a system under which the issue of notes is not confined to a single bank—does not of itself afford any security for "validity." Neither does the system of a Single Bank of Issue, although in this case the end may be attained more easily than in the former. All depends upon the conditions attached to the power of issue. But a system of plurality of issues insures steadiness of the measure of value much more fully than the system of a single bank of issue; for in the former case there is competition, which enables the law of supply and demand to operate in a normal

manner,—whereas in the latter case there is a monopoly, which tempts the privileged bank at times to keep the supply of currency below the requirements of the community, in order to obtain a higher price for it—a greater profit upon the issue of it.

Next, as regards an issue of State-notes. Such a system entirely secures the validity of the notes—because a State always, and naturally, makes its notes a legal tender: but whether or not the steadiness of the measure of value is maintained depends upon the principle adopted in the issue of those State-notes. A State-currency, in short, insures in the most perfect manner the validity of the note,—the notes being made a legal tender by Act of Parliament or by an Imperial decree; but it does not insure that the value of the currency, relatively to goods and other kinds of property, shall be always the same.

It is almost superfluous to say that if State-notes are issued simply in the form of Government expenditure, there is no security whatever for the steadiness of the measure of value. The monetary requirements of a community are dependent partly upon the amount of taxation, but mainly upon the condition of trade. And the monetary requirements of trade and the amount of Government taxation are not mutually dependent: so that a currency-system which is regulated by the latter only, cannot be adjusted for both. It is possible to conceive that a State-currency, limited by the amount of the Government expenditure, might be inadequate to the varying monetary requirements of the community,—there being no provision, under such a system, for an

enlargement of the issues when an increase occurs in the requirements of the public. But as a matter of fact, the special defect of a State-currency is of an opposite kind—namely, its liability to excess.

For example, in exceptional times—as in time of war—a Government may not be able to cover all its expenditure by means of taxation. It must have recourse to loans. And it is quite reasonable that, in the life of a nation, the exceptional seasons of war should borrow from the normal seasons of peace; just as a merchant in bad years must have recourse to a portion of the profits which he makes in ordinary times, and may even forestall, to some extent, the profits which he may reasonably reckon upon in the future. But when a Government has free power to issue currency, instead of contracting loans, it has every inducement to meet its extra expenditure by means of an increased issue of its notes: for in this way the Government obtains the required sum without any difficulty, and also without having to pay interest for it.

It is true that if this increased issue of State-notes were accompanied by an equal increase in the monetary requirements of the country, no depreciation of the currency would take place: in which case the result would be a pure gain alike to the Government and to the community. And doubtless an increase in the monetary requirements of the country generally does, to some extent, take place in such exceptional times as during a war: the very increase of the Government expenditure of itself occasioning an increased requirement for currency, in which the State-payments must be made.

Supposing that the general trade of the country be not diminished (and sometimes it is not) by the occurrence of war, then the war itself, by creating a new branch of trade, augments the monetary requirements of the community, and tends to absorb the extra issues of State-notes. Nevertheless, howsoever this cause may lessen the depreciation of the currency which naturally ensues from an extra issue of paper-money by the State (in lieu of contracting loans), it is very rarely, if ever, so potent as to prevent such a depreciation of the measure of value.

This constitutes a serious objection to a State-currency,—to a note-circulation of which the issue is in the hands of the Government. It is true that the community may actually lose no more (in the end it frequently loses less) from an over-issue of State-currency than if loans to the same amount were contracted; but the indirect effects of such an operation are exceedingly detrimental. The alteration and frequent fluctuations of the measure of value inflict great hardship upon individuals,—creditors losing and debtors gaining, and all contracts being vitiated. And when such a system of State-issues is carried to the length to which it has recently been carried in the United States, a widespread spirit of gambling is generated, which is inimical to the interests of honest industry, and demoralising in its effects upon the community at large.

But if not issued in this form—namely, as regulated in amount by the Government expenditure, and practically "inconvertible" (which is the only form in which a State-currency has ever yet been established in any country),—under what conditions is the issue to be

permitted, and in what manner are the State-notes to get into circulation? The two indispensable points are (1), that the State-notes be, like our present banking-currency, convertible into specie on demand; (2), that they be issued in such a manner as to respond freely to the requirements of the community,—increasing and diminishing in perfect accordance with those wants, so that the measure of value may not be subjected to fluctuations, always most embarrassing to the community, and sometimes fraught with most serious disaster.

Excluding from consideration the form of issue by means of Government expenditure, which is manifestly inadmissible, there are but two ways in which a State-issue of notes can be made. One of these is by the establishment of a State Bank, exercising all the powers and functions of ordinary banking—*i.e.*, receiving deposits, and dealing in loans and discounts. The other is, by establishing simply a Government office which shall issue State-notes to all the banks of the country, in exchange for specie and adequate securities, say Consols, and which in return shall engage to pay all the notes so issued in specie on demand.

The advocates of a State-currency have not as yet given any definite statement of the system which they desire to see established. For want of a better, we must take the latest edition of the programme (which has been revised and re-revised during the last twelve months) of the Currency Reform Association. This programme proposes the establishment of a State Bank, acting alike as a bank of deposit and as a bank of issue; and this establishment is expected to yield a large profit

to the State. It is to be the Bank of the State, receiving in deposit all the revenue payments of the country, and also, we infer, deposits from the public. It is also to issue notes of its own, which are to take the place of the present note-circulation of the banks; and these notes are to be handed over to the banks upon certain conditions, which have been altered and re-altered in each successive edition of the Association's prospectus, and which are still stated with much vagueness.

Now, first, as to this proposed State-establishment in its character as a bank of deposit. The Government moneys in bank—*i.e.*, the balance in hand of the revenue payments in excess of the Government expenditure—usually amount to about six millions sterling. What is the proposed State Bank to do with this large sum, and also with the deposits which it may receive from the public? Merely to keep this money in hand, idle and unprofitable, would never do. It would be a serious absorption of capital, which ought, as at present, to be employed in carrying on the national industry. It must be put into circulation. But how? The only way is, by means of loans and discounts—*i.e.*, in the purchase of commercial bills, and in making advances upon negotiable securities, such as shares, debentures, and bonds of various kinds. Fancy a State engaging in such operations. The prime business of a bank-manager is the valuation of negotiable property. He must know a good bill from a bad one; and also what securities it is safe for the bank to lend upon, and how much may be safely advanced upon them, after leaving a broad margin to meet the possible fluctuations in their market-value.

We do not believe that a State-establishment would conduct such trading operations so well as an ordinary bank would do: instead of making a gain on such operations, it is not unlikely that the State would sustain a loss. Moreover, the conduct of such a State Bank would be liable to the charge of favouritism. More or less at all times, but especially in critical times, a bank has to refuse some of the bills and securities offered to it—doing so upon no definite ground, save that the manager regards some men's credit, or the value of some securities, as greater than that of others. It is not a question of proof, but of opinion: the acceptance or rejection of a bill by a bank-manager is simply the result of a more or less accurate or inaccurate surmise. And yet upon this acceptance or rejection may depend the welfare or ruin of the party, whether an individual or a company, who thus applies for banking-accommodation. Again we say, fancy a State taking upon itself such a responsibility. It is out of the question. A State may exact some return from the bank with which the State-moneys are deposited; but the State cannot be its own banker: for in that case it would have to put its balance into circulation by means of loans and discounts,—a kind of business wholly unsuitable for it. And for the same reason it follows, *a fortiori*, that a State cannot be the banker of the public, by receiving deposits from the community.

Hence the idea of a State *Bank* is out of the question. The only feasible form of State-intervention in this matter is by means of an Issue establishment,—not a bank at all, whether of issue or of deposit,—but simply

a fountain of currency, from which the banks of the country can obtain a supply of notes in accordance with their varying requirements. The State cannot issue notes directly to the public,—for such an operation (as we have seen) would necessitate the State's engaging in loans and discounts; but the State may issue its notes to the banks, leaving the banks to issue them in loans and discounts to the public.

This, we say, is the only feasible form of State intervention in this matter: but let us see how such a system would work. We take for granted that the State-notes are, like the present bank-notes, to be convertible into specie on demand. And the first point that will strike any practical man is, that a State-issue of notes is much more likely to become inconvertible than if the notes were issued by banks. Individuals would have no means of enforcing payment in specie from the State in exchange for its notes. A bank must stop, must become bankrupt, if even in one single instance it does not pay coin for its notes on demand: but you cannot stop the State. This is an important consideration: especially when we reflect that every form of State paper-currency hitherto established has been inconvertible, and that such a currency must always be peculiarly liable to become so. But let us pass over this, and see what are the other conditions of such a system.

The State-notes are to be issued to the banks, and the State is to be liable to pay them in specie on demand. Hence it follows that, in issuing its notes to the banks, the State must at the same time take means to insure the convertibility of these notes. And the best, if not

the only practical way of doing this is to make the banks, in their purchase of notes from the State, pay an adequate proportion of the price in the form of specie. Accordingly, the grand point to be considered in a State system of note-issues is, the condition upon which these issues are to be made to the banks. To require that the banks shall pay for all the notes in specie is as impracticable as it would be unnecessary. Such a process would be a heavy loss to the country, and at the same time it would render the currency quite as inelastic as it is at present. (1) The whole amount of specie at present held by the banks in ordinary times is only twenty millions sterling, while the actual note-circulation of the banks amounts to nearly twice as much. Hence, if the State-establishment were only to issue its notes to the banks in exchange for an equal amount of specie, there would be an immediate and absolute loss to the country of twenty millions sterling. (2) Moreover, under such a condition of issue, the inelastic character of the currency, which at present is its greatest defect, and which is so productive of disaster, would be perpetuated. As experience has abundantly proved, a greatly increased requirement for notes on the part of the community may take place without any corresponding internal demand for specie. And if the banks, at such times, could only obtain a supply of notes by depositing with the State an *equal* amount of specie, a needless embarrassment would be occasioned, and also a costly one.

Putting aside, as alike injurious and impracticable, the plan of making the banks pay for a supply of State-

notes wholly in specie, we come to the best and more practicable plan of the banks paying to the State-establishment for a supply of notes partly in Government securities, and partly in specie. But in what proportions? If the proportion be fixed, then we shall have an inelastic currency as at present; and also, as is obvious, we may not have an adequate provision for the convertibility of the notes. The proportion of specie which is ample in ordinary times becomes inadequate in exceptional times. As the only means of meeting this difficulty, the Currency Reform Association propose that the State-establishment shall have power to alter the conditions of issue at its discretion. That is to say, it may demand from the banks a larger proportion of specie in exchange for its notes at some times than at others. On the hypothesis that such a State-currency be established, this is the only solution of the difficulty. There are times when more specie than usual is required by the public, and when accordingly the State must keep a larger amount of specie to secure the convertibility of its notes. And there are only two ways in which the State can make this provision: namely, either by making the banks deposit with the State a larger proportion of securities in exchange for the notes,—say by requiring £105 in Consols instead of £100,—and leaving the State to provide itself with the extra amount of specie required by selling its securities abroad; or else (as the Association proposes) by making the banks pay a larger proportion of specie for the notes which they require. Here again we find a most delicate and onerous responsibility thrown upon the Government. In all such

cases, the amount of specie required to insure convertibility of the notes is more or less a matter of opinion. The State-establishment of issue, like an ordinary bank, will naturally think first, if not entirely, of its own credit, and will probably over-provide itself with specie: and, in any case, it is the result alone which can decide what is an adequate provision, and what is an excessive one. At the time when the extra provision for the convertibility of the notes is made, the extent to which such a precautionary measure is requisite must always be a matter of conjecture. Consider, then, the magnitude of the responsibility thus thrown upon the Government office of issue, and indirectly, in truth we might say directly, upon the Government itself! In a crisis, banks may be ruined by being unable to obtain notes upon the high terms required by the State Office of Issue, and the fall of these banks will inflict tremendous losses not only upon their shareholders, but upon the commercial classes and the general public: and yet the result may prove that the higher terms then demanded by the State Office were unnecessary. What Government would choose to incur so grave a responsibility? In truth, whether or not the higher terms required by the State Office for the issue of its notes were really justifiable, it is so hard to *prove* that such terms were necessary that a loud outcry against the Government would be raised by the shareholders and customers of the fallen banks, as well as by the commercial classes at large, who would suffer severely from the contraction of credit, and from the collapse of industrial enterprise, which necessarily follow such bank-failures. The shareholders and de-

positors would attribute all their losses to the action of the State Office in refusing to supply notes on the ordinary terms; and all the trading classes would murmur. And probably in not a few cases the complaints would be well founded. Again we say, what Government would willingly incur so grave a responsibility, or expose itself to so great an amount of opprobrium? Even if the system of a State Office of Issue were in other respects the best—which we deny,—the tremendous responsibility which it would throw upon the Government would be fatal to the plan. No Ministry in its senses would undertake so delicate and so onerous a trust.

The real magnitude of the operations of such a State Office of Issue appears to be wholly overlooked. It seems to be imagined that such an office would be exposed to no greater demand for specie in the cashing of notes than is experienced by the banks at present. If this were the case, the functions of the office would be easily discharged. At present the demand for specie in exchange for notes is unimportant. Hardly more than £200,000 in coin is needed to meet all the demands for specie in connection with the note-circulation of the banks. Such demands, in fact, arise only from the necessity on the part of the public to obtain "small change,"—there being no notes in England of less value than £5. In Scotland, where £1 notes are issued, the demand for specie in exchange for notes is actually *nil*. But in the case of a State Office of Issue such as that above described—namely, one which should take upon itself the whole duty of securing the convertibility of its notes, making the issue of notes a trade upon which it

appropriates the profits,—the state of matters would be totally different. These State-notes would be a legal tender everywhere save when presented at the State Office. Accordingly, under such a system, the banks would be entirely relieved from the duty of making payments in specie, either to the note-holders or to their depositors. All that could be required of the banks would be payment of their liabilities in State-notes: and they certainly would not incur the heavy expense of keeping a stock of gold when there was no call for them to do so. The State Office of Issue would then hold the only metallic reserve in the country. Although receiving no deposits, *it would have to keep gold to meet the wants of all the banks of deposit in the kingdom.* Its notes would be taken by the banks, not merely to supply the community with currency (*i. e.*, notes), but also as a means of supplying their customers with specie. At present a depositor, or any one who gets a bill discounted, can obtain gold from the bank simply by drawing a cheque upon it for the required amount. But under the proposed system, he could not obtain gold from any bank: he could only get State-notes, which thereafter he must take or send to the State Office to be converted into coin or bullion. Hence the State Office would have to keep a stock of gold sufficient to meet all the foreign drains of specie as they arise.

Mark the consequences of such a system. In the first place, the Government would require to become a bullion-dealer, and also a dealer in foreign securities, on the largest scale. The Government would have to watch "the exchanges;" it would have to sell and buy

securities in the foreign Stock-market,—increasing or diminishing its stock of gold according to the varying requirements of the public. We do not think that this is a kind of business which a Government should undertake; neither do we think that any Ministry in this country would like to be saddled with such a responsibility. So much for the part which the Government would have to play in the matter. In the second place, consider the practical effect of such a system upon the community. Any note-holder who wished to get coin in exchange for notes would require to send his notes to London, and get them cashed at the State Office. Depositors would be in no better position: they could not demand a single sovereign from any bank in the kingdom. The banks would not keep gold—only State-notes; and their depositors would have to accept payment in those notes, and then send them to the State Office to be cashed. Suppose a summer tourist in Edinburgh wanted fifty or a hundred sovereigns to take with him on his excursion; he must first send his notes to London to be cashed, receiving the amount, we presume, in a registered parcel. Or—which is the more important form of the difficulty—if a Glasgow, Liverpool, or Belfast merchant required to export a certain amount of specie, he would have to do likewise. Specie would be unobtainable save at the counter of the State Issue-office in London. The inconvenience of the system would be simply intolerable. Moreover, even as a question of domestic currency, if the note is to remain convertible, clearly the gold should be kept at the places where it is needed. If the proposed State-notes were to be incon-

vertible (as all State-notes hitherto have been), there is no more to be said; but if they are really to be convertible, it is necessary that the means of convertibility (*i.e.*, the gold) should be kept, not merely in a State Office in London, but in all places of the kingdom where the cashing of notes may be desired. And if there are to be a hundred or more branches of this State-establishment throughout the country, the expense of such an arrangement would swallow up all the profits,—while the grander difficulties of the system would still remain undiminished.

To sum up. As has been shown, the project of a State *Bank* is out of the question—it is impracticable; because it would involve the Government in all the trading operations and risks of ordinary banking, which are unsuitable for a Government to undertake, and which would, moreover, impose upon it the gravest responsibilities. We have also shown that a State Office of Issue which should undertake to secure the convertibility of the note-circulation—although a much simpler project than that of a State Bank—is open to the following objections:—(1) As the conditions upon which it issued notes to the banks could not be regulated by a fixed rule, and must vary with the circumstances of the time (more specie being required from the banks on the issue of notes at some times than at others), such a method of issue would involve the Government in serious responsibility, exposing it at times to much popular opprobrium. (2) The State Office would have to keep gold to meet the wants of all the banks of deposit in the country. (3) The system would impose upon the Government the

necessity of acting as a bullion-dealer, and also of dealing by alternate sale and purchase in foreign securities. (4) The inconvenience of such a system to the community, unless branches of this State Office were established all over the country, which branches would probably swallow up all the profit of the arrangement. And (5), even if the State were to make a profit on the issue of its notes, this gain would be acquired simply by taking from the banks a portion of their present profits, and thereby would cause them to increase their charges upon the public for banking-accommodation. Thus, while the gain (if any) to the State from such a system of issue would be wholly illusory—having to be paid for by the community,—the difficulties and onerous responsibility which such a system would throw upon the Government are sufficient of themselves to prevent its adoption.

XIX.

MONETARY REFORM

THE first desideratum in the question of Monetary Reform is to devise a plan which will give to our monetary system a suitable power of expansion, to meet the severe strains which ever and anon are made upon it. How to obtain an elastic monetary system: this is the main problem with practical men. They care comparatively little as to the terms upon which this elasticity or expansibility is to be procured. They have become so accustomed to high rates of discount—eight, ten, or even twelve per cent—that they would be thankful if currency in adequate amount to the wants of the community could in times of difficulty be obtained even upon those exorbitant terms. The most pressing defect of the present system is, that even upon these terms an adequate supply of currency is not always to be obtained. At times, substantially good securities cannot be converted into currency; and mercantile houses, financial companies, and even banks, have to come to the ground

owing to a temporary impossibility of converting their assets into currency.

The second point to be attended to is, that under a perfect monetary system the value of the currency should always be the same. The currency is the Measure of Value—the circulating medium by which the value of all other kinds of property is represented in a negotiable form. If the currency fluctuates in value, all monetary contracts are thereby vitiated. Under the present system in this country, it is no exaggeration to say that a merchant who gives his bill or promise to pay £1000 three months after date, may find that, owing to a change in the value of money, he has to pay £1250; and it is quite a common case if he has to pay £1100 instead of £1000. Say that a merchant, when the Bank-rate is 4 or 5 per cent, purchases a thousand pounds' worth of goods, and gives a bill for £1000 payable at three months after date. In the interval, the Bank-rate may be raised to 9 or 10 per cent; in consequence, the markets are depressed to the extent of 20 or 25 per cent below their former ordinary price: and thus, in order to get money to meet his bill, the merchant must sell not only the thousand pounds' worth of goods which he received, but a fifth or a fourth part more, before he can obtain the £1000 which he promised to pay. This is a great evil. It indicates a glaring defect in our present monetary system. It is a barbarism.

The grand object of all plans of Monetary Reform is to prevent or minimise fluctuations in the Measure of Value,—in other words, to insure steadiness in the value of the currency, in which all contracts are made; so

that those contracts may not be vitiated owing to a change in the value of the circulating medium by which they are payable and must be discharged. It is of momentous importance to the community that the sum (the amount of currency) which a man promises to pay at a certain date—whether it be a yearly rent for house or land, or a three months' bill—should represent the same value or purchasing-power, should be convertible into the same quantity of merchandise or other property, at the time of payment as at the time when the contract was made.

It is impossible, of course, to prevent fluctuations in the value of the ordinary kinds of property; for all kinds of property vary more or less from time to time, and in some cases suddenly, owing to a change either in the amount of supply or in the extent of the demand. Such changes are inevitable, and no one imagines that they can be prevented. But what is desired is, that changes of prices should not be occasioned merely by a temporary excess or deficiency of the currency. The amount of the supply and the extent of the demand for any kind of property remaining the same, the price of that property should be unaltered. Yet at present, in such circumstances, the price of goods is vastly enhanced or lowered owing to a wholly extraneous cause—viz., the fluctuations in the Measure of Value, a change in the purchasing-power of the currency, owing to the supply of currency (as regulated by the Bank Acts) becoming greater or less than usual in proportion to the demand for it.

We cannot prevent fluctuations in the price of goods —corn, cotton, houses, or land,—because it is impossible

to increase the supply of these commodities at all times when the demand increases, or to diminish the demand for them at all times when the supply of them falls below the ordinary amount. If the harvest is bad, the price of corn must rise; so must the price of cotton, or any other kind of goods, if the supply from any cause falls short of the demand. In like manner, the price of corn or cotton, or any other commodity, must fall if, from any cause, the supply is greater than the usual demand. Such changes, we say, are acknowledged to be inevitable. But the value of the currency is another matter. Paper-money, especially in the form of banking-currency, is the offspring of civilisation, devised for the very purpose of keeping steady the Measure of Value: it is a means by which the supply of currency may be kept always commensurate with the demand for it,—increasing if the demand for it increase, and diminishing when the demand diminishes. When the community require more currency, they obtain it from the banks in the form of additional loans and discounts: if less currency is needed, fewer notes are thus taken from the banks. Hence it follows that if currency be issued by the banks always on the same terms —that is to say, if the Bank-rate, the charge for banking-accommodation, remains always the same — the Measure of Value will be perfect; the relative proportion between the amount of the currency and the requirements of the public will be always preserved; and consequently the purchasing-power of the currency (not indeed as regards any particular kind of goods, but as regards property in general) will at all times be alike,

—so that all monetary contracts will be equitably maintained, and no man will have to pay more value or receive less than he bargained for when his contracts were made. The attainment of this end is indispensable to a perfect monetary system. And it is the grand object which all currency-reformers have, or ought to have, specially in view.

There are two broad, and in some respects rough-and-ready, ways in which it has been sought or proposed to impart steadiness to the currency—*i.e.*, the Measure of Value. One of these is, by fixing the rate of discount; the other is, by fixing the amount of the currency. The former of those means was (substantially) in use in this country for nearly a century and a half after the establishment of banks and banking-currency; and it was adopted, *suâ sponte*, by the great Napoleon in founding the Bank of France. The latter system was advocated by Cobbett; it also finds favour with some writers of the present day. But neither of those systems is perfect of itself, and the latter is wholly untenable.

1.—The proposal of Cobbett—which is now advocated afresh—to preserve fixity in the Measure of Value by always keeping the currency fixed at a certain amount, although plausible in appearance, will not stand examination. The value of the currency (like that of every other thing) depends not merely upon the amount of the supply, but also upon the extent of the demand. There are two factors in the calculation, and Cobbett looked only at one. If the requirement for currency remained at all times the same, and if the amount of the supply remained likewise the same, the value of the currency

would consequently be perfectly steady. But, as every one knows, this is not the case. The requirement for currency varies greatly from time to time. Hence to fix the amount of the currency, instead of being a means of insuring its uniform value, would ever and anon cause its value to fluctuate to a serious extent. In truth, if the amount of the currency were fixed (though it is not easy to see how it could be absolutely fixed), our country would be subjected to even greater monetary embarrassments than at present. The defect of our present currency-system is a want of elasticity,—it cannot expand freely in accordance with the wants of the community; but if the currency were absolutely fixed in amount, we should be even worse off than we now are. Hence, whatever arguments may be advanced in support of a steady Bank-rate, as a means of insuring steadiness in the value of the currency, no such argument is tenable in support of fixing the *amount* of the currency. With a fixed amount of currency we could not possibly have a fixed or steady Bank-rate. The two things are incompatible.

2.—Napoleon I., when founding, or at least reconstituting, the Bank of France, said to the Governor and Directors: "Write up in letters of gold these words—What is the object of the Bank of France? *To discount commercial securities at four per cent.*" Quoting this maxim, and appealing also to the established practice in our own country previous to 1844, during which long period the Bank-rate never varied more than one per cent, some writers now propose that a legally-fixed Bank-rate should be substituted for the ceaseless fluctuations in the charge

for banking-accommodation which have prevailed under the new system, established by the Bank Acts of 1844-5. That such fluctuations are exceedingly detrimental to the interests of trade and industry of all kinds is indisputable. But the question is, How far is it practicable to abolish them, by establishing a fixed Bank-rate?

If the Bank-rate were fixed—if the charge for making loans and discounts to the public were always the same—the steadiness in value of the currency would be fully insured. For, in such a case, the cost to the public of obtaining currency would be at all times the same; so that the value of the currency would always be the same. Now, the desirableness of securing a uniform value for the currency is indisputable; and certainly, those who maintain that it is practicable to have a fixed Bank-rate, have a strong basis of facts to argue upon. They can point to the historical fact, that for 150 years after the establishment of Banking in this country, the Bank-rate never varied more than one per cent—ranging from 4 per cent to 5. Or they can point to the case of France, where, for half a century after the founding of the Bank of France by Napoleon I., a similar practice was steadily adhered to. In truth, it is a remarkable fact that, with a fixed Bank-rate of 4 per cent, specie-payments were fully maintained by the Bank of France during all the great wars and terrible national emergencies that took place during the reign of the First Napoleon. It is true that Napoleon always tried to make war support war, by levying forced contributions of money and supplies from the conquered countries; nevertheless, even after making allowance for this, it is a striking fact that the Bank of

France, during those critical years, should have never failed to meet its liabilities to pay specie on demand, while its charge for loans and discounts never altered from 4 per cent.

But a great change has taken place since then—indeed within the last quarter of a century—which must not be overlooked. It is only recently that the foreign trade of France has assumed large proportions; and the foreign trade of our own country has likewise attained a magnitude far exceeding that of former times. This vast expansion of International trade has occasioned a greater demand for specie—the only form of currency which is available in settlement of the international balances. Hence it may be argued that, although a fixed Bank-rate of 4 or 5 per cent was practicable in former times, when there was little international trade, it would be quite impracticable now. On the other hand, it is to be noted that the supply of specie, the annual addition to the world's stock of the precious metals, has since 1848 increased in a ratio quite equal to, if not greater than, the increase of international trade. In truth, the vast increase in international trade is in great part simply a consequence of the augmented supply of specie, without which such an expansion of trade could not have taken place. On the whole, therefore, it is very doubtful if there has been any change in the circumstances of the case sufficient to render a steady Bank-rate of 4 or 5 per cent a whit less practicable now than it was in former times. But there are other considerations which have to be taken into account, and which seriously conflict with the proposal for a legally-fixed Bank-rate.

The Bank-rate is, presumably, the charge at which Banks can profitably carry on their business,—which business is to supply the public with the banking-currency (notes and cheques) and specie, in exchange for good negotiable securities deposited with the banks. This charge represents the cost which a banking-company incurs in keeping up its establishment,—the rent of the premises, salaries of its clerks and managers, &c.; and also the cost of supplying banking-currency and specie in exchange for commercial currency (bills) and other kinds of negotiable property. The first item of this charge is easily understood; it is the *second* alone which requires elucidation. Banking-accommodation, as we have said, may be given either in bank-notes, or in cheques, or in specie; and the cost to the bank of giving this accommodation depends upon the extent to which the bank is drawn upon in one or other of those three ways. Thus:

(1) It is obvious that if the customers of the bank (the persons who deposit with it bills and other negotiable securities in exchange for a power of drawing upon it for the amount) take payment only by drawing cheques upon it, and if these cheques be paid into it again by the receivers, the process entails no expense upon the bank at all. In such a case the bank can discount bills to any extent at no expense to itself, save the ordinary cost of the establishment. Or if those cheques were paid into other banks, the result would be practically the same,—inasmuch as the cheques which each bank holds against its neighbours usually balance the cheques which its neighbours hold against it. Speaking roundly,

then, as long as the public take payment of the discounted bills, &c., only by drawing cheques, the process entails no cost upon the banks at all. (2) If payment of discounted bills, &c., be taken in the form of a bank's own notes, the cost to the bank in this case also is almost nominal; for the notes of a bank of good repute are *never* cashed, save (when no £1-notes are allowed to be issued) as a means of getting "small change." (3) On the other hand, if payment of the loans and discounts be demanded from the bank in specie, the cost of giving the accommodation is great. To meet such cases banks must keep in hand a stock of specie, which yields no interest; or they must provide themselves with specie by the sale of their securities (abroad), upon which a certain amount of loss may be incurred.

Now, it is true that, in ordinary times (as shown by the statistics of Sir John Lubbock*), fully nine-tenths of the drafts upon banks are made only in the form of cheque-payments—which occasion no cost to the banks at all. Nevertheless, banks are always *liable* to be called upon to pay the amount of their loans and discounts in specie,—so that they must keep a stock of the precious metals; and also at certain times this demand for specie becomes of serious magnitude, thereby rendering the giving of banking-accommodation a costly process. The inference from these facts is important. Since the demand for specie (which is the greatest element in the cost of banking) greatly varies from time to time, it appears impossible that the charge for bank-

* *Supra*, p. 6, 27.

ing-accommodation—in other words, the Bank-rate—can always remain the same.

Drains of specie from the banks arise wholly in connection with our Foreign trade and investments: the Home trade, which supplies by far the larger amount for loans and discounts, needing only cheques and notes. Now, it is true that those foreign drains of specie are merely exceptional occurrences,—specie usually flowing into this country in greater amount than it is exported. Hence it may be said—"Why do not the banks act accordingly? why do they not treat those foreign drains according to their real character—namely, as exceptional occurrences, which can be taken into account in fixing the charge for banking-accommodation? Why should not banks act as Life Assurance Companies do? When a visitation of the cholera or other deadly epidemic occurs, those companies do not charge more for insuring a man's life than in ordinary times: they adhere to their ordinary rate, which is calculated to meet those exceptional times. Why should not banks do the same?" It must be admitted that there is much to be said in favour of such a proposal. Moreover, it is not a novel one, for (as we have said) it was the established practice of our banks for a century and a half; and it worked with better results to the community than the new system of 1844 has done. The old system was this:—The banks found by experience how much specie was requisite to carry on their business safely, on the average of years; and they fixed their charge (the bank-rate) accordingly. They found that 4 or 5 per cent was adequate to do this; and they charged this rate at

all times. They did not raise their charge when an exceptional drain of specie took place; neither did they lower their charge when their power of giving banking-accommodation was greater than usual. They struck an average, and adhered to it,—just as a Life Insurance Company does.

This is unquestionably by far the better course as regards the interests of the community. And it is an intelligible and reasonable process as regards the banks. At the same time, on purely banking grounds (*i. e.*, apart from considerations of the public weal), it is more natural that banks should vary their charge according to the circumstances of the time,—raising it or lowering it in proportion as the cost of giving banking-accommodation to the public increases or diminishes. The banks may revert to the old system—which in point of principle there is nothing to object to: but what if they refuse to do this? Would it be right to compel them to do it by Act of Parliament? We think not: for in such a case Parliament would have to fix at a definite point the charge at which banking-accommodation is to be given; and we think that this is a matter which banks ought to be free to decide for themselves.

But then, there must be freedom and competition. If the State is not to interfere with the bank-rate, there must be no monopoly of the right of issue: there must be perfect freedom in banking as in other kinds of trade.

Monetary Reform may proceed either (1) upon a basis of notes convertible into specie on demand, or (2) of inconvertible notes made a valid tender by Act of Parlia-

ment. We shall consider the question under both shapes. Let us take the latter of those alternative courses first.

AN INCONVERTIBLE STATE-CURRENCY.

As a prelude to our exposition of this mode of monetary reform, we may say a word on the general principle of inconvertible paper-currency.

The necessity for a general suspension of payments in specie in any country only arises in exceptional times. Hitherto it has occurred chiefly, if not always, as a consequence of a great war. At such times it may arise from two different causes. It may arise either—as in England in 1797—in consequence of an unusual absorption of specie in military operations and in foreign loans connected with the war; or, as in France in 1793, and as recently in the United States, from the necessary expenditure of the Government exceeding not only the revenue but also the largest amount which the Government can obtain by means of loans. In this latter case, the Government makes up the deficiency of revenue by an issue of inconvertible State-notes —a process which is equivalent to a forced loan, to be gradually redeemed by the State after the country has returned to its normal condition of peace and prosperity. This case is in great part a political one; and it is more instructive to consider the other, which comes more purely within the consideration of monetary science.

When the operations of war and military loans

produce an excessive export of specie, the power of the banks to pay their liabilities in coin is gradually exhausted, and the result is a general suspension of specie-payments. The Government raises large loans, and withdraws the amount in specie from the banks for the purposes of export; the contractors who have to supply the army abroad act in like manner; until there is no more specie left in the banks. It is a demand for payment of deposits in specie which compels the banks to suspend cash-payments. The note-circulation of the banks (as shown in 1797) has nothing to do with it. It is true that as, when such a suspension takes place, the banks pay their depositors in notes, the note-circulation also must be made inconvertible, otherwise the process would be illusory. But as regards the note-circulation pure and simple, no specie is asked for it,—or only as a means of procuring "small change" in countries like France and England, where no small notes are allowed to be issued.

The inconvertibility of the note is unquestionably a great evil; nevertheless, in certain circumstances it is a lesser evil than others for which it affords a remedy. For example:—when (as in England during the great war with France under Napoleon I.) specie in some country rises exceptionally in value, owing to the unusual amount of it required to be sent abroad, the alternative arises, either to suspend cash-payments, or to restrict the usual loans and note-issues of the banks to such a degree as to enable those establishments to meet their liabilities in specie. The latter course is really impracticable: for a great contraction of loans (as in

England in 1797, and in a lesser degree in 1825, and in the United States in 1857) naturally produces such a panic and "run" for deposits on the banks that those establishments are forced to suspend specie-payments. An internal "run" for specie is produced by the panic, in addition to the external demand. The principle of self-preservation, in fact, leads every community in such circumstances to a suspension of specie-payments, as the only means of escaping a tremendous and most disastrous convulsion. Were the opposite course to be tried, what would follow? (1) The value of the currency and the rate of interest would be enormously raised. The whole monetary engagements of the community would be vitiated. One class would gain unjustly, and the others would lose unjustly. This would be a social revolution of the very worst kind. But this would not be all. For (2) the whole industrial energies of the country would be paralysed. The merchants, the manufacturers, and traders of all kinds (who carry on their business by the aid of credit) would be ruined. Producers and others, having to pay an exorbitant rate for their loans, would be unable to compete with those of other countries. And the export-trade, by a greater development of which alone could specie be brought into the country to replace the sums ceaselessly sent abroad to support the war, would be diminished beyond the ordinary amount.

Moreover, a suspension of specie-payments at such a time, what would it produce? Suppose all the specie in a country were withdrawn, and its place exactly supplied by notes, the currency would not be depre-

ciated in any way below its ordinary value. The notes would purchase exactly the same amount of goods or labour as the coins did. The currency would not *rise* in value with the abnormal price of specie; but it would maintain its usual value,—which is much better. Indeed, this is the very thing wanted. The notes would buy exactly as much as the coins did before—neither more nor less,—and just as the coins would do when they come back, when the currency returns to its normal condition.* And specie will so come back. It goes away, not owing to any depreciation of the currency, but because, as in England in 1797, there was an exceptional demand for it, in order to make payments abroad, which could only be made in specie. And the specie will come back in like manner,—without any rise in the value of the currency, and simply because the exceptional demand for specie has ceased.

True, the safeguard against over-issues which "convertibility" affords would be temporarily withdrawn: but it does not necessarily follow that over-issues would take place,—that the value of the currency would be depreciated below its former level. In judging of this matter, we must not confound two very different things. Issues of State paper-money—in the form of assignats or greenbacks—always depreciate the currency: not necessarily, it may be, but practically this has always been the result. Why? Because those State-notes are

* For example, this is what actually occurred in the United States in 1857. Moreover, the notes of the New York banks circulated freely at par—they were actually as good as English sovereigns or American eagles—during the whole time of the suspension of payments in specie.—*Vide supra*, p. 228.

an *addition* to the ordinary currency,—and the Government can issue any amount of them it pleases.

On the other hand, as we have previously shown,* a temporarily inconvertible Banking-currency is not so prone to such depreciation. In fact, we question whether any depreciation of the currency would take place, owing to the note-circulation being made temporarily inconvertible, so long as the notes were issued by banks, and not by the State. The notes, no doubt, might cease to be equal in value to specie,—but this can occur only when specie has exceptionally and temporarily risen in value. At such times, specie loses its prime quality as currency —namely, its steadiness of value; and still to adhere to it, in such circumstances, is to forget the real use of money, as the measure of value. The fact that a bit of metal was once a pint-pot is certainly no reason for continuing to use it as a measure after its cubical capacity has been altered. To adhere (if adherence were practicable) to specie-payments in those highly exceptional periods, would be to adhere to a means which has become ineffective, and which, in fact, has ceased to be a (proper) means at all. Logically absurd, the process, at the same time, would be practically disastrous. It would sacrifice alike the interests of the community and the power of the State.

Proposed Plans for an Inconvertible Currency.

So much for the general question. As regards the proposals now made for a reform of our monetary system by means of an inconvertible State-currency, what is

* *Supra*, p. 299, 300.

proposed, in order to keep steady the measure of value, is an issue of notes inconvertible into specie, but valid in payment of taxes and of all other payments to or by the State, and made a legal tender in all payments between man and man. There are various forms in which such a proposal has been made; but these (so far as they are entertainable at all) may be summed up under two heads:—

Firstly, there is the proposal that such an issue of inconvertible State-notes should be made to the amount of each year's taxation; the notes being cancelled when received by the State in payment of taxes, and fresh notes issued to the amount of the next year's taxation. Such a plan is manifestly based on the idea that, if the Government taxation amounts to 70 millions, an equal amount of notes will be needed in payment of taxes. But every practical man knows that this idea is totally unfounded. At present, of the 70 millions of taxation, certainly not one-tenth part is paid in notes,—nine-tenths being paid to the tax-collectors either in bank-cheques or in coin. And even if the inconvertible State-notes were to be for £1, still probably one-half of the taxation would be paid in cheques and coin. In fact, the amount of the Government taxation is no index whatsoever to the amount of money (notes and coin) required in revenue-payments: so that the principle upon which this proposal is based is wholly fallacious.

Secondly, It has been proposed that, instead of making those inconvertible State-issues equal in amount to each year's Government taxation, only a fixed amount (say 20 millions) of such notes be issued. Not

to raise theoretic difficulties, we may say frankly that we have no doubt that such notes would circulate as freely as bank-notes convertible into specie on demand. Neither shall we lay stress upon the fact that such inconvertible issues would import another anomaly into our already sufficiently anomalous monetary system. The banks, when a depositor applied to them for payment of a certain sum in specie, would be entitled to refuse, and would give him simply those inconvertible State-notes, leaving him to provide himself with specie as he best could. But, putting aside such objections, what, after all, would such a system accomplish? It would be a monetary gain of so many millions to the State; but it would not be of the slightest use as a remedy for our monetary difficulties.

It is quite obvious that an issue of inconvertible notes would effect a gain to the State, equal to the amount of those note-issues. It is also true that, if the amount of the note-issues were kept clearly within the amount of currency required by the country, those State-notes (although not legally convertible into specie) would circulate as freely as the convertible notes now issued by the banks. But this gain to the State would be just like that upon any issue of inconvertible paper-money,—like the assignats of France or the greenbacks of America, which were issued under the pressure of a great national emergency, and as a means of raising forced loans from the community. Every one knows how liable such a system is to abuse. But even supposing it were not abused—even supposing that no more State-notes were issued than would natu-

rally circulate at par with the specie which they represent,—still it is obvious that such a gain can be made only once. Those notes, being a legal tender, would take the place of coin. The banks would be entitled to pay the State-notes to their depositors instead of specie: accordingly, the banks would keep less specie on hand than at present: and the coin so displaced would be exported, or partially absorbed in jewellery and ornamentation, so as to be rendered unavailable for further use as currency. Such a gain, therefore, we repeat, could be made only once; and hence it ought to be reserved (as has been the case with all such inconvertible State-issues in other countries) as a resource in great national emergencies.

This gain to the State is the only advantage which such a system could accomplish. The system would not diminish in the slightest degree the defects of our present monetary system. It would not help us in the least to meet the fluctuations in the supply of gold which constitute the root of our ever-recurring difficulties. It would certainly set loose, once for all, a certain amount of gold at present held by the banks: but that gold would thereupon disappear from the circulation: and thereafter we should be in no better plight (if not in a worse one) than before, when a foreign drain of gold took place.

Hence, as a plan of monetary reform—as a means of remedying the defects of our present monetary system (and it is solely in this light that they are advocated),—the above-stated plans for an issue of inconvertible State-notes are wholly worthless. They are quite incapable

of meeting the *variations* which so frequently take place in the requirements for currency. Whether the issue of those inconvertible notes were to vary with the Government expenditure, or were to be fixed in amount, the root of the evil, the chief cause of the present changes in the measure of value, would remain wholly unaffected. In both cases there would be a gain to the State—and more or less to the community,—as these notes would take the place of an equal amount of coin; but in neither case would there be any remedy for the fluctuations in the value of the currency, which in both cases is the special object sought to be attained.

A Better Plan.

Neither of those plans, we say, is admissible, seeing that they afford no remedy for the great variations in the value of the currency, which are the worst evils of the present system. But there is one way—as we shall now show—in which a State-issue of inconvertible notes might be adopted so as to remedy this defect, by insuring stability in the value of the currency. It is as follows:—In the first place, the State must issue these notes to the banks,—leaving the banks thereafter to issue them to the public in the form of loans and discounts, to an amount corresponding with the actual requirements of the community. Secondly, the conditions of issue by the State should be that the banks, in exchange for a supply of those notes, shall deposit with the State an equal (or somewhat larger) amount of Government securities. The notes, since they would thus come to represent Government Debt, would be received by the State in

payment of taxation, &c.;—on this ground, and also because their substantial value is secured by a deposit of State-securities, they may also be made a legal tender throughout the community; and finally, in the event of a bank becoming insolvent, the State will return to the creditors the Government securities which the insolvent bank had deposited in exchange for the notes. Thirdly, all the banks would then hold their reserves (as a means of securing a supply of notes) in Consols, instead of by a credit at the Bank of England. Each bank, in short, would then keep its own reserve (which is the right plan); and, moreover, this course would be more profitable for the banks than the present system, inasmuch as they would get 3 per cent interest upon their reserves (as interest on their stock of Consols), instead of no interest at all, as is the case with the amount which they keep in reserve in the Bank of England.

Now let us see how such a system would work.

1. The banks, as a whole, would hardly require to make any addition to their stock of Government securities. The Bank of England at present holds fully 27 millions of Government stock (15 millions in its Issue department, and fully 12 in its Banking department); and the other banks of the kingdom, taken together, probably hold at least 15 millions of Government securities;—in all, fully 42 millions, which is more than equal to the whole amount of bank-notes at present required by the community. But even say that the banks were to keep ten millions more in the form of Government securities than at present, as a reserve for supplying themselves with notes: this amount would suffice

to meet the largest possible increase in the monetary requirements of the community,—and yet the gradual purchase of this amount of Consols by the various banks would be so small an affair, that it would make no appreciable change in the price of the Funds. If the National Debt of this country were of small amount, the purchase of Consols necessary on the adoption of the new system might have a considerable effect on the price of the Funds: though only in a beneficial form—namely, by enhancing their price, by increasing the demand for them; but this effect (which some persons might object to, even though it is beneficial to the State) could not be produced by the gradual purchase of merely ten millions of Consols by the banks, seeing that the amount of the Funds is so great (nearly 800 millions), and also that upwards of 200 millions of this Government stock are sold and bought every year even in ordinary times.

2. The banks would obtain 3 per cent interest on their stock of Government securities,—just as any private person, or non-trader, would do; and thereafter they would obtain, as profit on their issue-business, the amount of the Bank-rate, minus the costs of this kind of business.

3. Whatever might be the fair rate of profit on such note-issues (which would soon be settled by the action of free competition among the banks), one important result would be accomplished. The bank-rate would remain steady. The cost to the banks of obtaining a supply of notes would always be the same,—hence their power of supplying these notes to the public would always be

the same: as a natural consequence, their charge for the supply would likewise be the same at all times. Of course, this would not prevent banks charging a higher rate than the ordinary one for risky loans,—if they chose to engage in such business; just as they at present charge for such advances higher terms than the "bank-rate," or ordinary charge for banking-accommodation. But the *ordinary* charge, or bank-rate, under this new system, would, owing to the causes above stated, be always steady, if not absolutely uniform.

4. As a corollary, or concomitant result of this new system, the amount of the currency would always be exactly commensurate with the requirements of the community,—increasing or diminishing with the variations in those requirements: so that the measure of value would be maintained, free from all fluctuations. The public would never take more notes than they required from the banks, seeing that they have to pay for a supply of those notes; while the banks have a direct interest in keeping the rate of discount as high as possible.

5. Under this system, the precious metals (gold and silver) would resume their natural place as ordinary commodities. They would be bought and sold just like corn, cotton, coal, or iron. Like these and all other commodities, they would sometimes rise in value, sometimes fall. But those variations in their market-price would no longer suffice to alter, as at present, the measure of value,—which would then be simply the State-secured note-circulation. The note-circulation would then remain perfectly steady in value, and the

contracts between man and man would be freed from the anomalies produced by the present variations of the currency. Men would then have no more difficulty in providing themselves with gold or silver than they have at present in buying corn or cotton, or any other kind of property.

Such, in brief, is a very effective plan of monetary reform, upon the basis of a system of a State-secured inconvertible currency. Since several writers, both at present and in past times, have suggested the adoption of an inconvertible currency-system, in various ways, all of which appear to us objectionable and unworkable, we propound this plan of our own, as one which not only renders the adoption of an inconvertible currency perfectly practicable, but in many respects advantageous. At the same time we need not give an exposition of this plan in detail, for we do not believe that the country is ripe for such a system: nor is so great a change requisite to put our monetary system on a satisfactory footing. Hence it is not in this form that we advocate a change in our monetary laws.

A CONVERTIBLE BANKING-CURRENCY.

Under a system of monopoly, the State is not only justified in interfering with the Bank-rate, but it is imperatively called upon to do so in the interests of the community. This principle is fully recognised and acted upon in France and Belgium, in each of which countries the power of issuing notes is confined to one

privileged bank. In those countries, the State, while conferring this monopoly, takes care to prevent its abuse. The Banks of France and Belgium are not allowed to profit by charging more than 6 per cent upon their business-transactions—upon the loans and discounts which they make to the public. If they think it needful for their own safety to charge more than this rate, they are perfectly at liberty to do so; but their shareholders are not allowed to pocket the gains made by this extra charge. After the crisis of 1857, the Bank of France for some years adopted the practice of the Bank of England, in raising its charge for banking-accommodation whenever a drain of specie occurred, though it never carried out this practice to the same extent as the Bank of England. But experience has shown the fallaciousness of this system, and for three years past the Bank of France has repudiated it—nor is it likely that it will ever again have recourse to it. The Bank of France has found (what is also sufficiently proved by the experience of the Bank of England) that a great elevation of the bank-rate has no effect in attracting specie from other countries, yet produces widespread distress at home. In fact, a great elevation of the bank-rate, by ruining traders and shaking credit, actually intensifies in some cases the foreign drain of specie, by destroying the credit of bills, and thereby inducing other countries to demand payment from us in specie instead of in bills.

A monopoly of the right of issuing banking-currency in the form of notes exists also in this country, though not to the same extent as in France; yet the State

takes no means of guarding against the abuse of this monopoly. The right of issuing bank-notes is restricted to those banks which issued notes previous to 1844; and the restriction has also been made in such a way as to give a practical monopoly to the Bank of England. No other great bank in England is allowed to issue notes at all: it is only the small banks in the provinces which are permitted to issue notes; and, moreover, they are not allowed to extend their issues upon any terms beyond the average of their note-circulation in 1844. The great London banks, which alone could effectually compete with the Bank of England, are entirely prohibited from issuing notes of their own: they have to go to the Bank of England for a supply of notes whenever an unusual demand for such currency takes place. The Bank of England is allowed to issue 15 millions of notes upon Government securities,—a power which is wholly denied to all its great rivals.

Such being the case, the State would be perfectly justified in imposing a limit upon the rate of profit which the Bank of England makes upon its loans and discounts. And, if the present system were to be maintained, we think that the State, in the interests of the community, ought unquestionably to take this course.

But we look for a remedy in another direction. The system of Monopoly is wholly out of date: it has been abolished in every kind of trade except banking. And we are confident, not only that the system of monopoly ought to be abolished in banking also, but that it will be so abolished at no distant date. Hence, we look for a remedy of the great fluctuations and inordinate eleva-

tions of the bank-rate (which have been the bane of this country since 1844)—not to a system of regulated monopoly—not to a perpetuation of the present system of monopoly, safeguarded by a limit imposed by the State,—but to the abolition of monopoly altogether, and to the adoption of the principle of free-trade and competition in banking, combined with certain other conditions, which appear to us requisite for the establishment of a perfect system of Convertible Banking-currency.

XX.

FREE-TRADE IN BANKING

FREEDOM and competition are as much needed in banking as in other trades. The rate of discount, the charge for money on loan, can only be maintained at its natural level by a system of free-trade in banking,—by a system under which every bank, subject to the same conditions, shall have the power of issuing bank-notes in answer to the requirements of the public: so that there may be the same freedom and competition in the supply of banking-accommodation as there is in all other kinds of trade. Such an abolition of the present system of restriction and monopoly in our monetary affairs—such an application of the principle of free-trade to banking in all its functions—will be as genial in its effects upon the national wellbeing as the advent of spring, relaxing the icy fetters of a protracted winter. And if it be accompanied, as we trust it will, by the adoption of an international monetary system,* the adoption of

* See *infra*, Chap. XXIII.

this new monetary system will constitute a never-to-be-forgotten era in the ever-onward progress of civilisation.

What, then, are the conditions under which a system of free-trade in banking may be safely and advantageously adopted?

The issue of notes is a natural function of Banking.* It has been an essential feature of banking ever since the introduction of paper-money. And in this country, the prime object for which banks were established, and their chief function until in recent times, was the issue of notes. Hence without an equal right to issue banking-currency (notes), there can be no free-trade in banking.

These are three different modes in which a free system of banking can be established; and in order to make my exposition complete, I give plans consonant with each of them.

One of these proceeds on the basis of an Inconvertible note-currency. For the benefit of advanced currency-reformers, and also with a regard to the future, I have given a plan of this kind in the previous chapter.† The other two plans proceed on the basis of a Convertible note-currency: and I shall now state them.

One of these is to revert to the old and long-established system in this country, under which banks were allowed to issue notes as a natural part of their business, —but with a new condition, to the effect that the notes

* *Vide supra*, p. 119-22, and 272-73.

† The principles of an Inconvertible currency-system—namely, of a currency invested with independent value, and not based upon specie—were fully discussed in the chapter, "What is a Pound?" in my work on the *Economy of Capital*, p. 444-56,—which, as there stated, was a reprint from a previous publication of mine in 1858.

shall hereafter constitute a first claim upon the assets of the bank which issues them. For my own part, this condition seems to me all that is requisite to be imposed upon the banks as they now exist. In Scotland, where banking was left perfectly free from the first, the note-circulation proved perfectly trustworthy throughout the century and a half prior to 1844. And though the case was different in England, this was entirely due to the monopoly of joint-stock banking obtained by the Bank of England in 1708,—which monopoly prevented the establishment of large banks. In consequence, instead of banking being conducted in England (as in Scotland) by a comparatively small number of great banks, with branches all over the country, a multitude of petty banks sprang up, with no resources adequate to withstand the slightest monetary pressure. At one time, we believe, there were nearly a thousand of these petty banks in England; and, as a matter of course, they gave way in scores whenever a crisis occurred. The banks which thus fell, it is true, were not all insolvent,—that is to say, many of them had assets equal to their liabilities: but then, they held no reserves adequate to provide themselves with more specie when a run upon them took place for payment of their deposits,—the deposits, and not the note-issues, being the prime cause of their fall. This was the true cause of the unsoundness of the English banking-system, and consequently of the English note-currency.* Had banking in England been left free, as it was in Scotland, it would doubtless have attained the same happy results. Get

* *Vide supra*, p. 276-78.

sound banks, and the soundness of the note-circulation naturally follows.

The English banks, we believe, although still, as a whole, inferior in solidity to those of Scotland and Ireland, are sufficiently strong to be intrusted with the right to exercise their natural function of issuing notes. Among the English provincial banks of issue are to be found establishments as small as any other banks in the kingdom. Yet the note-circulation of the English provincial banks maintained its credit unshaken during the terrible crisis of last year, and also during the previous crises of 1847 and 1857. Hence I believe that the right of issue might be restored to all the English banks, with no other condition than that the notes should rank as a first claim upon the assets of the banks. In truth, with the exception of the Bank of England, the notes are but a mere driblet of a bank's liabilities: so that even in the case of a thoroughly bad failure, they could be paid at once out of the assets of the fallen bank. And if thus secured, by a priority of claim, the credit of the notes as currency would not be questioned.

I might adduce other arguments in support of this plan, and especially the evidence of facts, drawn from the experience of other countries, as well as of our own. I might also suggest, as an additional safeguard, the adoption of measures for the further strengthening of the English banks by the process of consolidation—to be afterwards mentioned. But it is needless to develop this plan in detail, as it is not the one which, with deference to existing circumstances, I prefer to recommend. In questions relating to the currency, above

all others, it is necessary to take into careful account the prevailing sentiments—even if they be but prejudices. Accordingly, while I think it right to submit in outline the two above-stated plans of currency-reform, the scheme which I propose for immediate adoption (and which was briefly suggested in my previous work*) is one by which the system of free-trade in banking is carefully safeguarded, and put in harmony with the sentiments as well as with the wants of the public.

Let us proceed, then, to show alike the principles and the provisions of the new monetary system which we propose as one in full harmony with the spirit of the times and the requirements of the community.

As regards the Deposits in banks, it is allowed on all hands that legislative interference is unjustifiable, and would be injurious. It would be as much out of place for the State to make banks find security for their deposits, as it would be for the State to make a demand upon a merchant to give public security for the solvency of his operations. The deposit of capital with a bank is as voluntary an act as the sale of goods to a merchant upon credit. In the one case, as in the other, the transaction is a purely voluntary one,—as to the expediency of which individuals must judge for themselves. This was the opinion decidedly expressed by Sir R. Peel in 1844, and there cannot be a doubt as to its correctness.

But the issue of notes stands on another footing.

* See the *Economy of Capital*, p. 357-58.

Bank-notes are currency; and although any man may *de jure* be at liberty to refuse to accept them in payment, *de facto* they must be so accepted, if trade is to be carried on in its usual course. Hence the State is entitled to take means to insure the validity of bank-issues, seeing that these notes constitute a large portion of the currency of the country, and that any doubt as to their value would produce a widespread embarrassment. Accordingly, while adopting a system of perfect freedom of issue, as the only means of maintaining the measure of value and the rate of interest in their natural condition, measures should be taken to secure the value of those note-issues by an adequate guarantee. And such a system can be most fully attained by the issue of notes convertible into coin (as at present) by the banks which issue them, but also based upon an equal amount of State-securities,—combined with perfect freedom of competition in the issue and employment of those notes.

The general principle of such a system would be as follows:—That the State Office be empowered to issue notes to any bank which purchases and deposits with it an equal (or somewhat larger) amount of Government securities. These Government securities, or any portion of them, to be returned to the bank (or, in the case of a bank's insolvency, to the note-holders) on its giving back the notes issued upon the deposit of, and in exchange for, these securities.

All banks alike to have an equal right to a supply of notes upon these terms. And each bank to be bound to maintain the convertibility of its issues,—in other

words, to pay its notes in specie when required to do so. But the State to fix no rules for the amount of specie to be held by any bank. In point of fact, a fixed rule would be inapplicable, and wholly mischievous. The circumstances of each bank are so different that a rule which might be proper for some banks would be quite inapplicable to others. The cases would differ, mainly from the different nature of the business carried on by each bank,—some banks, owing to the class of customers who deal with them, being more liable to a demand for gold in payment of loans and of discounted bills than others. But also, there is this great point to be kept in view. The proportion of specie requisite to support a note-circulation is not a fixed quantity, but varies with the circumstances, and especially with the extent, of each bank's circulation. Experience alone can show the proper proportion of specie which a bank must keep on hand to insure the convertibility of its notes. And all experience shows that the larger the amount of a bank's note-issues, the smaller is the *proportion* of specie actually needed to meet the demands for coin in payment of notes. Whatever be the amount of specie requisite to support a note-circulation of half a million sterling, a much smaller proportion is needed to cover a note-circulation, like that of the Banks of England and France, amounting to twenty or thirty millions. And the reason is obvious. Notes are only needed for home use; and, so long as a bank is known to be thoroughly solvent (or when, as under the New System, it is known that the value of the notes is amply secured), the pub-

lic never lose faith in the notes, never demand payment of them in specie, except as a means of obtaining "change,"—and this only in the case of England, where the lowest denomination of notes is £5. Hence, as a matter of fact, one-tenth or even one-twentieth of specie suffices to insure the convertibility of the note-issues of the Banks of England and France as perfectly as one-fifth of specie would do for a bank whose circulation amounted only to half a million.*

Thus, no rule can be laid down as to the proportion of specie which a bank should keep in order to insure the convertibility of its note-issues. The proportion naturally varies with the circumstances of each bank. And for the Legislature to fix the amount of specie to be kept by banks would not only be objectionable as a matter of principle, but productive of serious injustice and injury. Let the substantial value of every bank's issues be secured by an adequate guarantee (an equal amount of Consols); but let each bank look after the convertibility of its notes on its own responsibility, and in the manner which by experience it finds to be best.

Under such a system, the Validity of the Note would be amply insured. The notes would be secured by a more than equal amount of Government stock—the steadiest and most readily convertible of all kinds of property—kept in a State Office, and especially appro-

* As will be observed, we are here speaking only of the Note-issues and the cashing of Notes. As we have fully pointed out elsewhere (p. 150-52 and 162), all the great demands upon the banks for specie arise in connection with their Deposits and Discount-business, and would take place to the same extent though the banks did not issue notes at all.

priated for the note-holders, whoever they might be: so that even in times of panic and banking-failures the notes would still circulate freely,—the "cashing" of notes at such times (which even at present is quite trifling) then ceasing altogether, or nearly so. At the same time the convertibility of these notes would be as perfect as now,—the banks being bound to pay specie for them on demand, under penalty of bankruptcy.

The other great requisite of a monetary system—namely, the Steadiness of the Measure of Value—would also be secured to a greater degree by this new system than in any other way. The State would have no power of itself to increase or diminish the paper-money of the country. And the banks would have no motive for getting notes from the State except in response to an adequate demand on the part of the public. In this way we should escape the defects of a purely State-currency, which is always liable to an excess of note-issues,—owing to the inducement which a State has to meet any extraordinary expenditure by means of an issue of its own notes, in lieu of contracting loans.* And we should equally escape the evils of a monopoly of the right of issue, such as now prevails in this country: under which there is a tendency to contract the currency, in order to enhance the value of the commodity (money) in which banks deal,—banks having as great an interest in keeping money scarce as farmers have in limiting the supply of corn.

Under the system now proposed, the community itself would regulate the amount of the currency. There would be neither more nor less paper-money in circu-

* *Vide supra*, p. 296-97.

lation than the community desired. Unless more currency were required, the public would not take any additional amount of notes from the banks. Such an addition to the currency could only take place in the form of loans and discounts; and the public, it is obvious, would not pay for loans unless more money were required. Neither would loans be taken from any bank whose credit was not good: for of what use to the borrower could be a loan in notes if those notes would not circulate?

Hence such a system as we propose would respond perfectly to the varying wants of the community, and would thereby keep steady the measure of value in which all contracts are made; while at the same time it would secure the validity of the currency, alike by the new State-security upon which the notes would be issued, and by the free power on the part of the community to demand gold in exchange for the notes from the banks which issued them. The *whole* note-circulation of the country would thereby be placed on a solid basis;* and at the same time the currency would be allowed to expand and contract freely with the varying circumstances of the community. Every bank, we repeat, would, as at present, be bound to pay gold for its notes and deposits when required,—with the additional safeguard that all the notes would be secured by an equal, or somewhat larger, amount of Consols.

* For the incongruous conditions of issue at present in force, see *supra*, p. 270-71, and 280-81.

OBJECTIONS MET.

Before proceeding further, it may be advantageous to consider the objections to the New System which may arise in the mind of the reader: more especially as in answering these possible objections we can best give our remaining explanations.

(1.) As our system proposes that the banks, while allowed to issue notes upon the Consols which they deposit in the Government Office, should at the same time obtain interest upon these Consols just as a private individual, or non-trader, would do, it may be objected that this would give the banks of issue a double profit from the possession of Consols: that is to say, the banks, while getting the usual interest on these Government securities, would also get a profit on the notes which they issued upon such securities. This objection is quite untenable. The extra profit which the banks would thus make upon their Consols is due to the fact that they *trade* with those securities,—they make them a basis of their issue-business. This is only just: it is only what occurs with all wealth invested in trade. The man who invests his wealth in trade does not thereby part with his wealth,—he transmutes it (say) into a factory; and thereupon he obtains not only the current rate of interest on wealth unemployed by its owner—say 3 or 4 per cent,—but 5, 10, or even 20 per cent in addition, as a profit on his trading with that amount of wealth. Or again, suppose a merchant keeps a balance of £1000 at his banker's; upon this

security (so to call it) the bank will discount bills for him, or make advances to him, to ten times that amount,—at the same time paying to him interest on that balance. So that, by keeping £1000 in bank, he can trade to nine times more than that amount;—by which means the profit on that thousand pounds is nine times greater than if he kept it in simple deposit in bank. In like manner, it is only natural that banks which deposit Consols with a State Office as a basis of their issue-business, should, in addition to the usual interest on those securities, obtain a trading-profit upon the amount. Exactly as is the case at present with 14 millions of the Government securities held by the Bank of England, upon which as a basis it is allowed to issue an equal amount of notes.

(2.) The next objection which may be started is, that under such a system the note-circulation might become "redundant." "Redundancy" is a vague phrase; but the only practical meaning we can attach to it is, that the note-circulation would become depreciated in value compared to gold. Yet this objection is obviously untenable,—seeing that all notes issued under the New System, as at present, are to be convertible into gold on demand. Now, whether we regard the question theoretically, or by the light of experience, it is impossible for "convertible" notes ever to fall below the value of the coin which they represent, and into which they are convertible on demand. No man will take payment from a bank in notes whose value is below par; and if such a depreciation took place in notes already issued—*i. e.*, in circulation,—the moment the note-holder found that

the notes would not buy as much property (goods or labour) as the coins which they represented, he would immediately present the notes at the bank to be exchanged for specie. This is so obvious that no more need be said.

(3.) But there is another form which this objection may take. It may be said that under the New System the Bank-rate might be permanently lowered,—*i.e.*, the average charge for banking-accommodation might be lower than under the present system. In a national point of view, this is certainly not a result to be deprecated. The effect would simply be that the banks would gain less, and the community at large (or at least the industrial and producing classes) would gain more. Trade would then have to pay a less proportion of its profits to the banks than at present. In so far as this would be a consequence of the New System, the National Industry would be greatly benefited. A steady low rate of discount is the greatest adjuvant of Trade and of Production which any country can possess. *Cæteris paribus*, the country where the rate of discount is lowest has an advantage above all its neighbours, alike socially and commercially: it can give more employment to the working-classes, and it can command the markets of the world by supplying goods more cheaply than any of its neighbours can do.* Hence, even were this objection well-founded, it would constitute a very strong argument in favour of our system.

The fact that the New System would render impossible the exorbitant elevations of the Bank-rate which

* See also *supra*, p. 189-91.

too frequently occur in this country, we admit: this, indeed, is one of the great advantages for the sake of which we so urgently advocate its adoption. But that the New System would lower the *average* rate of discount in this country, to any great extent, we see no reason to believe. It could only do so by greatly reducing the profits of banking: and if it did this, what would follow? Simply, that less capital would be invested in banking than at present: the supply of banking-accommodation would be reduced, until the rate of discount rose again to a remunerative point. If banking in this country can be carried on profitably with a permanent Bank-rate of 2 per cent, good and well: so much the better for the country. If not, less capital would thenceforth be invested in banking-business, till the rate rose again to a remunerative level.

This really disposes of the objection. But let us consider the grounds upon which it is advanced. It may be said,—Since the banks get 3 per cent upon the Consols which constitute the basis of their note-issues,—and since the costs of the banks in connection with an issue-business, and also of keeping gold sufficient for cashing the notes, in most cases would not exceed 1 per cent,*—it might be advantageous to the banks to issue notes even though they made only 1 per cent of profit on this part of their business: that is to say, they might issue their notes at only 2 per cent. To this statement we have to reply, in the first place, that this rate is actually

* I reckon the costs of the Bank of England in connection with its note-circulation at 1 per cent; and in the case of the other banks, the cost of issue would probably be nearly the same. See Appendix.

higher than that which prevails at the present hour. The Bank of England itself charges no more than 2 per cent; and the other London banks are charging only $1\frac{1}{4}$ to $1\frac{1}{2}$. And yet, so far from the country being inundated with bank-notes, the banks, even upon those terms, cannot get the public to take loans from them to anything like the ordinary amount,—the loans and discounts of the Bank of England, for example, being at present fully 20 per cent below their average amount.

In the second place, this objection proceeds on the idea that the issue of notes would be the chief source of a bank's gains. This is true of the Bank of England; but it is not true of any other bank in the kingdom,—and least of all in the case of any of the present banks of deposit which might avail themselves of the new power of issue. The chief profit of all the banks (save the Bank of England) arises from their Deposits. Now if a bank (say the London and Westminster) were, under the New System, to issue notes of its own, it is true it might make a small profit by issuing those notes at 2 per cent: but what would follow? Why, *it would have to lend out the whole amount of its Deposits at the same low rate.* Hence, in ordinary times, it would make a great loss by so doing. Take the average rate of discount at 4 per cent, and say that the London and Westminster Bank were to get a million of notes of its own into circulation by issuing them at 2 per cent. Taking its profit on these note-issues at 1 per cent, the gain to the bank on this part of its business would be £10,000 per annum. But the Bank would simultaneously have to lend out its 20 millions of Deposits at the same rate: this would

be a loss of 2 per cent on 20 millions = £400,000! It is needless to say that no bank would take such a course. It is the first object of all banks to keep the rate of discount as high as possible: and they may be as easily trusted not to lend their money too cheaply as any other class of traders may be trusted not to sell their goods at too low a price. The system of freedom in banking which we advocate will, by means of competition, tend to keep the Bank-rate from becoming exorbitant, but it cannot possibly make the banks carry on their business at too low a rate to be profitable to themselves.

Experience is worth a bushel of theories: and what does experience in this matter show? For a century and a half, the banks of this country were allowed to issue notes of their own without restriction as to amount, and without being legally obliged to keep any security for their notes at all. Nevertheless, even under that system the Bank-rate never fell below 4 per cent! Moreover, during that long period, the note-business of the banks was far larger in proportion to the amount of their Deposits than at present. In fact, the issue of notes at that time was the main source of a bank's profits; so that the banks had then a far stronger inducement to get out their notes by charging a low rate of discount, than now (and especially under the New System, whereby a deposit of Consols is required), when the issue of notes forms but a very small portion of a bank's gains. When a bank cannot lend all its deposits at 4 per cent, why should it still further lower the rate by issuing notes at 2 per cent?

It is a striking proof of the want of practical knowledge which exists on this point, as indeed in almost all departments of monetary science, that one of our most eminent statesmen, especially eminent in financial reputation, when a suggestion was made to him for the adoption of a free issue of "convertible" notes based upon a deposit of Government securities to an equal amount, replied, "Why, there are 800 millions of our Government securities: what is to prevent an issue of notes to a like amount?" It seemed to him possible (not to say probable) that the note-circulation might actually be increased to the extent of 800 millions! It is needless to point out the absurdity of such an idea. The actual facts relating to note-issues, as already stated, amply demonstrate that there can be no over-issue of notes which are convertible into specie: nay more, that even under a system of inconvertible banking-currency (which we do not propose) the banks have a direct interest in limiting their note-issues, by keeping the rate of discount as high as possible. In fact, our proposed requirement for a deposit of Consols by all banks of issue simply furnishes an additional security for the note-circulation: for example, no legal security of any kind is at present attached to the notes of the English provincial banks of issue,—nor are they even liable to pay their notes or deposits in coin, Bank of England notes being a legal tender.

But let us add a word to show the stringency of the natural limitations which exist upon any addition to our note-circulation in ordinary times. In ordinary times, the present amount of our note-circulation suffices (or

nearly suffices*) for all the wants of the community. And unless more notes are required by the community, none will be taken from the banks, even if those establishments be eager to issue them. The present time is a proof of the impossibility of increasing the note-circulation when no more notes are needed. Even with a bank-rate of barely 2 per cent, the note-circulation of the country, as a whole, is almost the same as usual. On the other hand, when more notes were needed, as during the panic of last year, the note-circulation reached the highest point it has ever attained, although the minimum Bank-rate was then 10 per cent. When more notes are needed, the public must have them at any cost, in order to avoid bankruptcy. On the other hand, when no more notes are needed, the public will not take them upon any terms,—even (as seen at present) at an average bank-rate of only $1\frac{1}{2}$ per cent. This is only natural. When the public want more notes, they have to pay for them: and it is needless to say, they will not pay for what they do not require. And if more notes be really needed, their issue only serves to keep the bank-rate, and with it the value of the currency, at its existing level. Consequently it is only when the bank-rate is above its ordinary level — above the point which is amply remunerative to the banks—that those establishments have any motive for increasing their note-issues.

This brings us to the important advantage of the New System. Although the banks have no motive for ex-

* As previously stated (see Chap. II.) there is an annual absorption of 4 or 5 millions of specie into the coinage,—in consequence chiefly of there being no £1-notes allowed in England.

tending their note-issues when the rate of discount is low (the trifling gain which they might make by an increased issue of notes at such times being far exceeded by the loss which they would incur upon their purely banking-business), seeing that such an extension of their note-issues would only tend to perpetuate the low rate of discount; nevertheless the case would be different when from any cause the rate of discount tended to rise above its ordinary level. At such times, under the New System, some banks would deposit more Consols with the State Office, in order to increase their note-issues, and would continue to discount at the same rate as usual, seeking a profit from an extension of their business. Any bank might raise its charge as it pleased; but it would be kept in check by the competition of its neighbours. Under the New System, any bank would be free to charge 6, 8, or 10 per cent for its accommodation to the public; but, on the other hand, any bank might continue to issue its notes at a lower charge, and seek profit by acquiring a portion of the business of those banks which charged a higher rate than was necessary. As experience amply shows, banking in this country is a profitable business when the rate of discount is 4 per cent. Hence the moment the Bank-rate tended to rise above 4 or 5 per cent, some banks would content themselves with conducting their business at the ordinary rate; so that other banks which wished to raise their charge beyond an ordinarily remunerative point, would be kept in check by the fear of losing a portion of their business.

Banks, we repeat, like all traders, may be trusted to look after their own interests. There need be no more

fear of their charging too little for the use of their money than there is of a farmer selling his corn at a lower price than he can get for it. This will be the case under every system. But the advantage of the New System is, that it abolishes the present regime of Restriction and Monopoly—it subjects every bank to the healthy influence of competition,—and thereby allows the Rate of Discount to follow its natural course, *i.e.*, in accordance with the natural law of Supply and Demand.

Having thus cleared away the objections which might possibly be raised against the leading principles of the New System, we shall now proceed with our further statement of the plan.

ADDITIONAL PROPOSALS.

Under the New System, we should also propose (1) that all banks of issue should be constituted upon the joint-stock principle; (2) that no bank should be allowed to issue notes unless it had a paid-up capital of (say) £100,000;* and (3) that in order to secure a reserve to meet great emergencies, its "subscribed" capital (in the case of banks on the "limited" principle) should at all times exceed its "paid-up" capital to the extent of at least one-third.

* We have not the statistics requisite for the fixing of the minimum amount of paid-up capital for a bank of issue. In fixing this amount, deference must be paid to the existing rights of the English provincial banks, which alone would be affected by this new condition. The amount should be sufficiently large to promote a consolidation of those banks into larger establishments, yet without imposing upon them any great hardship.

We do not regard such conditions as indispensable: but, if adopted, they would have a beneficial effect upon the provincial banking-system of England, by tending to effect a consolidation of some of those banks,—thereby effecting an economy of their resources, while adding to their strength. Instead of having, as at present, a great number of small local banks, it would be better to have a smaller number of large establishments, with branches throughout the adjoining districts. Of course, in the case of the existing provincial banks of issue in England, time must be given (say two or three years) to allow of such consolidations being effected. It were unwise by Act of Parliament to force the work of consolidation beyond the point requisite to create sufficiently strong establishments: but this change might be carried to almost any extent by simply raising the minimum amount of capital which the banks of issue are called upon to hold. Some of the small banks of issue, it is true, might meet the change by adding to their capital: but, in by far the greater number of cases, they would prefer to have recourse to the process of consolidation,—in other words, several of the existing private banks of issue in England would join together, so as to form a joint-stock company, with one head-establishment, and branches in all the other places where they carried on their business.

The State-secured notes to be issued under the New System might bear on one side the State-label (so to call it), stating the value of the note,—the fact that it is secured by a deposit of Consols,—and also that it is a legal tender in all payments to the State. On the

other side the note might bear the label of the bank which issues it to the public, stating that the bank undertakes to pay it in coin of the realm on demand. As a matter of fact, these notes would seldom, if ever, be presented to the bank which issued them for payment in coin, save as a means of getting "small change." And this for two reasons. First, because (as has been repeatedly stated) when specie is wanted, it is obtained from the banks not by collecting and cashing a quantity of notes, but simply by drawing a cheque upon a bank and demanding the required amount in specie. Secondly, because the security of the deposited Consols, as well as the fact that the notes are a legal tender in all dues and other payments to the State, would render the notes acceptable at all times,—even in the exceptional case of the bank which issued them becoming insolvent.

The denomination of the notes to be issued is a matter of detail. There is no fixed minimum for the value of notes at present. Scotland and Ireland have £1-notes, England has no note below £5. The £1-notes are found to produce no embarrassment, and effect a great economy, in Scotland and Ireland; nevertheless that is not an adequate reason for summarily introducing them into England. The reason for the prohibition of notes below £5 in England was this:—The English banks of issue (always excepting the Bank of England) were in the main imperfectly constituted; and instead of placing them on a sounder footing, by allowing them to adopt the joint-stock principle, or by imposing certain safeguards on their issue of notes, the State practically limited the circulation of their notes to

the middle classes. In England, the middle classes are so trained to business, that they can judge for themselves what banks are to be trusted or distrusted ; and they have full power to reject the notes of any bank, save the Bank of England. But it was held that the working-classes, partly from inferior intelligence, partly from their position, which virtually compels them to accept any bank-notes tendered to them by their employers in payment of wages, ought to be protected against the possibility of having bad currency thrust upon them. Hence the prohibition against the issue of notes under £5 : a £5-note being too large a sum to be payable in weekly wages. But if the currency were secured in the manner which we have proposed,—if all banks of issue were established on the joint-stock principle, and if their note-issues were secured by an ample amount of Government stock,—the reason for prohibiting notes under £5 would be at an end.

As a matter of economical science, £1-notes might be introduced with perfect safety, and with a great saving to the community. On the other hand, as a question of State-policy, we should not advocate an immediate issue of £1-notes. If such small notes were adopted, there would be no use for the mass of sovereigns circulating in England ; and these would gradually be exported as bullion. By such a change, of course, the country would at once make a clear gain of fully sixty millions sterling, besides escaping the yearly cost for loss and wear of the coinage. But as a nation we are immensely rich, and we ought not hastily to reap an advantage which is sure to come in a more advantageous form if

we wait. An issue of £1-notes will certainly come in due course, either as a permanent system, or to meet a temporary exigency. During the closing months of the Crimean war (notably in November and December 1855), the demand for gold to supply the wants of our army abroad, and to make the Turkish and Sardinian loans, was so great, that the propriety of issuing £1-notes was publicly discussed and seriously thought of. And if the war had lasted for another year, we believe such a step would have become necessary. Now, the Crimean war was really a small affair. It was only two years of warfare at the most. We shall be very glad indeed, if even a war of that duration have no place in our future annals. But no one expects that such will be our fate, unless he bury himself in illusions,—as the ostrich is said to bury its head in the sand, believing itself safe simply because it has hid the danger from view. And it is obvious that should this country again be involved in a serious foreign war, when a large amount of specie will be suddenly required, it will be an immense advantage for us to have at hand, and readily available, these sixty or more millions of gold coinage, which only remain in circulation on the condition that small notes are prohibited. On this ground, therefore—as a question of State-policy,—we do not advocate in present circumstances the adoption of a £1-note circulation in England. In due time this step will be taken from necessity—owing to some State-emergency; and by merely waiting, we shall arrive at a result (an issue of £1-notes) which is desirable on the principles of economical science, without prematurely availing ourselves of

a large stock of specie which, in times of foreign war, would be an immense source of strength and power to the State.

Nevertheless, though we hesitate to recommend an *immediate* issue of £1-notes in England, we strongly advise an issue of smaller notes than those at present permitted. Although we do not desire to reduce the amount of gold-coin in circulation, we think it is advisable to render unnecessary any addition to that amount. And such an addition takes place, and must take place, under the present system. It goes on from year to year. Owing to the steady increase of retail payments, for wages and shopping-purchases, more gold is being yearly added to the currency, in consequence of the £5-notes being unserviceable in the making of such small payments.* To reduce the denomination of the English note to £2 might be too great a change for the simple attainment of the object we have in view; to reduce it to £3 would be an awkward change, and one also hardly worth making. The best plan would be to authorise the issue of notes for £2½: which would suffice to prevent any further absorption of gold in our domestic circulation, while it would not diminish, at least to any great extent, the amount of coins already in use. This, we repeat, would be the wisest course to adopt. It is true, the plan of reducing the denomination of the note in England to £1, as is the case in Scotland and Ireland, has the attractive merit of simplicity. Nevertheless, for the reasons of State-policy above mentioned, we think that a smaller change than

* See Chap. II.

this would, for the present, be the preferable course. An issue of £1-notes in England, we repeat, will come ere long; but the adoption of such a system may advantageously be delayed until it is called for as an effective means of meeting a great national emergency.

Some other results of the New System remain to be noticed:—

I. Every joint-stock bank which chose to make use of the right of issue would thereafter trade with its own notes instead of with those of the Bank of England. Nor would it be necessary for it (as at present) to keep a portion of its reserve at the Bank of England for the purpose of obtaining an additional supply of notes when required,—seeing that a bank could always obtain more notes by increasing its deposit of Consols in the Government Issue-Office.

II. Neither would any bank of issue require to keep a reserve at the Bank of England for "clearing" purposes. At present, as is well known, the balances at the Clearing-House are settled by cheques upon the Bank of England: the result being that a portion of one bank's reserve at the Bank of England is transferred to the credit of some other banks. Under the New System the Clearing-House would naturally become a department of the State "Issue-Office" (maintained at the expense of the banks who made use of it); and the balances would be settled by the transfer of so much Government Stock from the credit of one bank to another's. The Scotch banks already adopt the plan of settling their balances by transfers of Government Se-

curities: and under the New System this practice would be still more efficient, seeing that the Consols so transferred would be as good as notes,—the banks then having a power of converting those Consols into notes at their pleasure.

III. Under this system the banks would be induced largely to increase the most effective portion of their reserves,—seeing that they would then get 3 per cent interest on the amount (kept in the form of Consols convertible at will into State-secured notes), instead of no interest at all, as is the case with the reserves which they at present keep in the Bank of England. This is a most important consideration: for such a change would greatly increase the strength and resources of the banks.

IV. Every bank would keep for itself the amount of specie necessary to carry on its ordinary business. As regards the notes, less specie would be required than at present, seeing that State-secured notes would maintain their value under all circumstances: that is to say, even if a bank's credit were shaken, the noteholders would not make a rush for gold, knowing that the substantial value of the notes was amply and thoroughly secured. But under the New System—as at present—the banks would be liable to exceptionally heavy demands for specie in connection with their deposits and discount-business, at times when more specie than usual was needed for export. At present they meet such requirements by selling a portion of their securities, and then drawing upon the Bank of England for the amount of specie. In the case of many banks

there would probably be no change in this respect. The Bank of England would remain, not indeed the sole, but the chief reservoir of gold: an arrangement which is more economical than if the *entire* amount of specie were dispersed among all the banks of the country, and one also which is unobjectionable in other respects if kept within due bounds,—which, as we shall show, it would be by the conditions of the New System.

Each bank, indeed, might keep on hand a stock of gold equal to all the demands likely to be made upon it; or, if the bank were largely connected with foreign trade, it might attain the same end by keeping a stock of securities abroad, which it could convert by sale into specie. But no bank willingly keeps on hand more specie than is needed to meet its ordinary requirements: it prefers to keep a stock of securities (bearing interest) which it can, by sale, convert into specie when wanted; and in all cases at present, a bank contents itself with keeping the securities of our own Government, and selling them (when necessary) in our own market, and then goes to the Bank of England for the amount in specie. The Bank of England in this respect incurs no other liability than that which attaches to all banks,—it is simply liable to pay its notes and deposits in gold on demand: nevertheless, practically, the present system imposes an enormous responsibility and costly duty upon the Bank. Under the New System, however,—the "legal tender" character of its notes being abolished,—this hardship would cease; for the Bank could then, when in need of gold, make as effective a demand for gold upon the other banks as the other banks can do

upon it. At present the Bank of England is debarred from doing so, in regard to the other English banks,—for these banks can pay it in its own notes (these being a legal tender): but under the New System the Bank of England could, by selling its securities, demand gold from the other banks in whose notes or cheques it received payment, just as the other banks can now do in regard to it. This would be a sufficient check (if such were needed) upon the other banks, and an ample defence for the Bank of England.

V. Under the New System, all the banks would be required to publish periodical returns. At what periods those returns should be called for, and what items ought to be embraced in those returns, is a matter of detail which we need not here discuss. As all banks alike would have the power to issue notes, all of them might be required to make perfectly similar returns. At the same time, it is to be remembered that, under the system proposed, or under any conceivable system, just as under the present one, the Bank of England would occupy *de facto* an exceptional position. Under a century and a half of monopoly, its note-issues have increased far beyond the amount which otherwise it could have obtained. The New System would not alter this fact. The Bank of England, under the new regime, would start with a note-circulation exceeding that of all the other banks of the United Kingdom put together. Therefore, the returns required from the Bank of England might be fuller, and at shorter periods, than those required from the other banks. But supposing that the minor banks of issue published balance-

sheets only half-yearly, as the joint-stock banks do at present, or quarterly, or even monthly, there is one point which we think ought to be attended to,—namely this, that the returns should show not only the amount of specie, notes in circulation, reserve of securities, &c., for the last day or week of the period, but also the average of those items for each week during the entire period. Unless this be done, the returns of the banks may be so made up as to give no correct index of their condition.

INFLUENCE OF THE NEW SYSTEM.

The influence of such a system upon the Rate of Interest is obvious, and the effects of that influence would be most important. All banks having equally a means of lending their capital and utilising their credit, the rate of interest would be freed from the vicious action of a monopoly, and would immediately find its natural level under a system of freedom and competition. No bank would lend its money at too low a rate, any more than a merchant or shopkeeper would sell his wares too cheap. Every bank would seek to charge its customers as much as possible for the use of its notes. On the other hand, each bank would seek to extend its business, by accommodating the public so far as its own interests would allow: just as a merchant may accept a lower rate of profit, when by so doing he can secure a larger amount of business. And thus, under a system of free competition, the charge for money on loan would be regulated on the same principle as the price of other

commodities, and would find its natural level in accordance with the law of supply and demand.

Practically, the effects of this system would be mainly observable in the different course which banks would adopt in regard to supplying themselves with specie to meet the requirements of their customers. At present, whenever an unusual demand for gold for export occurs, in connection with our foreign trade or with investments in loans and industrial undertakings abroad, the Bank of England throws the whole of the burden, the cost of this banking-embarrassment, upon the shoulders of Trade;* and as the Bank possesses a virtual monopoly of the currency—no other bank or banks of issue being sufficiently powerful to compete with it,—all the banking establishments now contentedly follow its example. But under the New System—if that can be called new which is but a revival of the old in an improved form,—the case would be different. The case would stand thus. Each bank would then, as now, be at liberty to refuse any bills, the discounting of which would entail upon it a greater loss than gain. Banks know pretty

* For example, at any moment during the three critical months of 1866, the Bank of England might have borrowed five millions in gold (or twice that amount, if it had wished), upon security of the Government Stock which it keeps in its Banking department, from the Bank of France, which establishment was simultaneously suffering from a plethora of specie. But the Bank of England did nothing of the kind: it did not stir a finger to provide itself with more gold in order that it might extend its note-issues. The consequence was that for three months our commercial and manufacturing classes were oppressed by a *minimum* bank-rate of 10 per cent, while their French competitors were only paying 3½ per cent. What would be said if wheat in France were selling at 35s. the quarter, while in England it was selling at £5 the quarter? Under a right monetary system, the former case would be as impossible as the latter is.

well the class of bills for which, when discounted, payment is likely to be demanded in specie: in fact, such bills are, at any given time, generally confined to one particular branch of our foreign trade. And the banks would be at liberty to charge any rate they pleased for discounting such bills,—subject, of course, to the competition of their neighbours. Any bank which charged too high terms for such advances would lose its customers. And the result would be this: Banks, for their own interest, would then provide themselves with more gold at those times, in order to carry on their discount-operations. If they were to say — as the Bank of England says at present—"We shall not take any steps to provide the extra amount of specie which is required: we shall make you (Trade) do it at your own cost and loss;" then some other bank would offer to share with Trade a part of the loss, and would provide itself with gold in order to maintain or extend its discount-business. In this way, Trade and the Banks would settle the matter between them on fair terms, and the rate of discount would follow its natural course.

Drains of specie from banks are made almost entirely by means of Discounts,—by discounting commercial bills and withdrawing the amount in specie. But in the case of foreign loans, or unusually large investments in industrial enterprises abroad, a demand sometimes arises for payment of the ordinary banking Deposits in specie. Subscribers to foreign loans, or shareholders in foreign railways, &c., sometimes call up a portion of their deposits in specie, in order to obtain a supply of the international currency which is requisite to carry on such

operations. The effect of the New System would be substantially the same in this case as in the other. The banks, instead of availing themselves of the monopoly which they at present possess, and throwing all the burden upon the public, would have to deal fairly and minimise the difficulty; because, under a system of free competition, if any banks charged more than was reasonable, other banks would be ready to deal upon a lower scale of profits,—seeking an increase of profits not from higher charges, but from an extension of business.

Once released from the evil and artificial influence of a monopoly, in short, the Rate of Interest would follow its natural course. The rate would certainly not be fixed under the system which we propose, although its variations would be infinitesimal compared with what they are at present. Under the new system, the rate of interest would in each case be accordant with the nature of the business carried on. For example, a bank which deals with agricultural customers, or others connected simply with the Home trade, would require to keep on hand a comparatively small amount of gold; for any such banks are not affected by foreign drains of specie. In discounting the bills of its customers, or making advances to them upon securities, such a bank could always reckon that payment would be demanded from it only in notes,—seeing that notes alone are needed as domestic currency. It could also, for the same reason, reckon that payment of its deposits would only be called for in the same form. On the other hand, banks which deal with merchants connected with the Foreign

trade, or with capitalists who frequently embark a portion of their wealth in foreign investments, would require to keep on hand, or at call, a comparatively large stock of specie. The latter class of banks might reasonably charge higher terms for their discounts than those which were connected with the Home trade, —in order to compensate for the larger amount of specie which they have to keep on hand. Nevertheless, under the pressure of free competition, they would seek to meet the demands of their customers, and carry on their business, with as little outlay for dead-stock as possible. They would have recourse to the most economical means of providing specie when required. Instead of keeping a large stock of gold on hand (lying unproductive in their vaults), they would keep a portion of their banking-reserve in the form of interest-bearing stock at Calcutta, Paris, New York, or such other places as their customers were most in the habit of dealing with; so that, when any customer required to transmit money to those places, the bank would give him a bill or draft upon its agents there, which would serve the same purpose as specie.

Hence—and this is a most important feature of the New System—*the cost to the banks of cashing a portion of their foreign securities would constitute the only cause for raising the Bank-rate.* The rise of the Bank-rate, in fact, would only take place to such an extent as to recompense the banks for the loss, if any, which they might sustain in supplying themselves with more specie,—say by the sale of a portion of their reserve of foreign Stock. Even say that there was a consider-

able loss upon such sales. Say, for example, that the Bank of England were in need of five millions of gold, and that, in order to procure this amount of specie, it had to incur a loss of $1\frac{1}{2}$ per cent, or £75,000. This is an exaggerated estimate of the loss on such operations: indeed, Mr Reuben Browning* states that in 1825 Baron Rothschild supplied upwards of nine millions of specie to the Bank of England upon those terms (and nowadays the same operation could be effected at much less cost). Well, then, a rise of the Bank-rate to the extent of even $\frac{1}{2}$ per cent would more than cover the whole cost of that transaction! As the loan and discount business of the Bank of England ordinarily amounts to fully 20 millions sterling, a rise of merely $\frac{1}{2}$ per cent—say from $4\frac{1}{2}$ to 5 per cent—would suffice to yield to the Bank £100,000 in twelve months, as a set-off against the £75,000 which it spent in supplying itself with the five millions of additional specie.

Such, in outline, is our plan of Monetary Reform. We have likewise proposed two other plans,—one of them of very much wider scope than this: but we desire to keep the reform which we recommend for adoption within as narrow limits as is compatible with the attainment of a monetary system adequate to the wants of the community. It is a measure which would alike secure the validity of the Note-circulation, and keep steady the Measure of Value. The antiquated and injurious system of monopoly would also be replaced by a system of perfect freedom and equality.

* *The Currency.* By Reuben Browning. P. 34.

At the same time, the currency of this country would acquire that elasticity which is so greatly wanted, and which would enable us to tide over with ease those temporary difficulties which thrice during the last twenty years, under the present vicious and obsolete system, have inflicted such terrible disasters upon the community, and which tend to damage the credit of the country.

XXI.

REFORM OF THE BANK OF ENGLAND

THE Bank of England, the head and centre of our system of currency and banking, is an establishment *per se*. It is an anomaly. Legislation has done its worst upon it,—has conferred upon it so many privileges, and imposed upon it so many burdens, that both the position and the constitution of the establishment are wholly unnatural. The Bank acquired a virtual monopoly 160 years ago, in return for a loan which it then made to the Government. In consideration of that loan, the Bank was constituted the sole joint-stock bank of issue in England. And at successive intervals it purchased a renewal of this monopoly by making to the Government new loans. Those loans form part of the assets of the establishment; and in consequence, the amount of the Bank's surplus capital, or assets kept in reserve, has swollen into disproportionate magnitude to the amount of business carried on by the Bank. The result of this—especially since 1844, when the Bank's

power of extending its business was artificially restricted —has been most injurious. As every one knows, the larger the amount of a bank's capital compared to the amount of its business, the higher must be the rate of profit at which the bank carries on its business, if it is to pay an ordinary dividend. In brief, the capital invested in the Bank of England has been swollen to its present magnitude not by the natural requirements of the Bank's business, but as a means of purchasing renewals of its monopoly: and this disproportionate magnitude of its reserve-wealth is a direct and special cause why the Bank should seek to reimburse itself by enhancing its charges upon the community. If the amount of capital invested in the Bank were less, or if the extent of its operations were enlarged, it is obvious that the Bank could conduct its business at a lower rate of interest without any diminution of its profits. A rate of 4 per cent, for example, might then yield it as much profit as a 6 per cent rate does at present.

Let us then, in reviewing the present condition of the Bank of England, begin with the amount of its Assets, and see what relation these bear to its Liabilities, —or, in other words, to the amount of business which it carries on. At present the position of the Bank, with its unparalleled stock of gold and its small amount of business, is quite exceptional:* it would not be fair to take it as the basis of our exposition, however much it

* At present (September 28, 1867) the Bank holds 24½ millions of Specie, and almost 28 millions of Government securities; and its Liabilities to the public consist of 23¾ millions of Notes in circulation, and 27 millions of Deposits (the Public deposits being now at their highest). Its loans and discounts only amount to 17 millions.

would lend force to our remarks. We shall therefore deal only with the average statistics of the establishment in the years previous to the crisis of 1866.

GENERAL POSITION OF THE BANK.

The Bank keeps permanently on hand Government securities of various kinds to the amount of fully £26,000,000; also, on the average, nearly £15,000,000 of specie: making a total of £41,000,000. It also holds on the average upwards of £20,000,000 of private securities, consisting chiefly of commercial bills. Thus the Assets of the Bank amount in ordinary times to about £61,000,000. Its Liabilities consist of its note-circulation, averaging £22,000,000, and its public and private deposits, amounting to about £20,000,000: in all, about £42,000,000. So that, while holding 61 millions of assets, the Bank has only 42 millions of liabilities. It has one-half more capital than the total amount of business which it carries on.

Next, let us see the nature of its business and of its Liabilities. Rather more than one-half of its liabilities, as we have seen, consists of its

Note-Circulation.

With the exception of an infinitesimal fraction, its Note-circulation never becomes a charge upon the Bank at all. The notes issued are all needed to carry on the business of the country. The country—that is to say, the public and the other banks—must

have fully twenty millions of those notes, otherwise all business would be stopped. The notes are never brought to the Bank to be cashed save for the purpose of getting "change." As no notes are issued by the Bank for a smaller amount than £5, it daily happens that some note-holders want to exchange £5 or £10 notes for "small change,"—*i. e.*, coin: but this, and this only, is the extent of the demand for gold in payment of notes. And the amount of specie needed for this purpose in "the Hall" of the Issue Department amounts ordinarily only to a few thousands a-day.

The Note-circulation varies in amount,—sometimes rising above 25 millions, sometimes falling to 19 millions: but those variations are not occasioned by any cashing of the notes. Say that the note-circulation from any cause has reached 25 millions: what happens when five millions of the notes relapse into the Bank, and the note-circulation falls to a low point? As a matter of fact, such a change is very gradual, extending over a year or more. But, gradual or not, what takes place? Do the holders of the notes, when they no longer require them, take the notes to the Bank to be exchanged for gold? Not at all. The notes are simply paid in, either directly or through other banks, in the shape of Deposits. Their lapse is not occasioned or attended by the least demand for specie. When no longer needed, the notes simply filter back into the bank which issued them.

What is more, the demand for the Bank's notes on the part of the public is, as a matter of fact, in no way dependent upon the amount of gold in the

Bank. On the contrary, the Bank's note-issues are sometimes at a maximum when its stock of gold is at a minimum. As the most remarkable case of this kind (the most remarkable at least since the resumption of cash-payments), we may refer to December 1825, at the height of the great crisis of that year, when the Bank's note-circulation rose to $25\frac{1}{2}$ millions, while the Bank's stock of specie had fallen to *one million!* And never at any time in the history of the Bank were its notes more eagerly sought after by the public. The same fact was exemplified to a lesser extent during the crisis of 1857, and also in 1866,—despite the efforts of the Bank to prevent it, by charging an exorbitant rate for the use of its notes. In fact, as the experience of every monetary crisis shows, the public never lose faith in the note-circulation: they accept the notes as readily when (as in 1825) there is hardly a sovereign in the Bank, as when the vaults of the establishment are overstocked with gold.

The most erroneous ideas have prevailed, and to some extent still prevail, in regard to this part of monetary science. The originators of the present Bank Acts held that the ever-recurrent drains of specie to which this country is subject were occasioned by an "over-issue" of bank-notes, whereby our paper-money became depreciated,—whereupon the note-holders (it was further believed) took the notes to the Bank to be exchanged for gold, and then exported the gold. A more baseless theory (as a better knowledge of the facts has since shown) never was imagined. Never at any time since the resumption of cash-payments in 1819 has the paper-

money of this country been depreciated; nor indeed is it ever possible for any convertible currency, such as our present bank-notes, to fall below their specie-value.

The fanciful dogma upon which the present Bank Acts were founded is now known to be an illusion, an absurdity. Nevertheless, several erroneous notions in regard to the note-circulation are still entertained by writers on monetary science,—simply because those writers prefer to theorise in the dark, rather than investigate the facts. For example, we are frequently told in print that the way in which gold is withdrawn from the Bank, whether for export or for domestic use, is by getting a large amount of the Bank's notes and then cashing them at the Issue Office. This is a mistake. When a drain of gold occurs, it takes place quite irrespective of the Bank's notes. Notes are never used in this way. The drains would occur just the same, and to the same extent, though the Bank did not issue notes at all. A drain of gold is made just in the same way as a demand for notes,—that is to say, by means of cheques. A bank, or an individual who keeps an account at the Bank, draws upon the establishment in the usual way, and receives the amount either in gold or in notes as he pleases. If a private customer hands in a cheque, the usual question is, "How will you take it?" —*i.e.*, in notes or in gold?—and if he wishes 50 or 100 or 200 sovereigns, he gets it at once across the counter of the Banking Department. On the other hand, if a bank or merchant wishes to have a large sum in gold, he presents his cheque and receives an order upon the

Bullion Office for the amount. If he wishes to have (say) half a million in gold, the Bank does not go through the clumsy process of first giving him half a million in notes, and then sending him to the Issue Department to get those notes exchanged for gold. In short, notes play no part at all in the drains of gold from the Bank. And we here state exactly how such drains of gold are made, in order that this long-established fallacy may receive its quietus.

Thus, dealing simply with facts, we find that the only demand to which the Bank is exposed in connection with its Note-circulation (which constitutes fully one-half of its entire Liabilities) arises from its notes being too large to be of service in retail payments,—thereby producing a trifling cashing of notes (a few thousand pounds a-day) for small change. For a century at least, and during the most terrible monetary crises on record, this and this only is the extent of the demand to which the Bank is exposed in connection with its note-issues.

The Deposits.

Nearly one-third of the Deposits of the Bank of England consist of the Government moneys intrusted to its keeping; and these are deposited and withdrawn with a regularity which makes it easy for the Bank to deal with them. The other portion consists of the deposits of private customers, but chiefly of the other banks,—many banks keeping a portion of their reserves in this form.

In regard to these Deposits, whether public or private, which constitute the liabilities of the Bank in its purely

banking-department, we have (at the present stage of our inquiry) to consider them simply in relation to the *amount* of the Bank's assets,—*i. e.*, irrespective of the *form*, whether bullion or convertible securities, in which the amount of wealth with which the Bank carries on its business is kept.

And the first point to be observed is this,—that a withdrawal of deposits, while it diminishes the assets of a bank, equally diminishes its liabilities. A diminution of a bank's deposits, like a decrease of its note-issues, lessens the amount of business which the bank carries on; but it causes no diminution in the amount of the bank's assets compared to the amount of its liabilities. On the contrary, in the case of the Bank of England—and of every other bank which has a surplus,—any decrease in the extent of the bank's business or liabilities simply increases the ratio of its remaining assets to its remaining liabilities. For example, suppose that ten millions of the Bank of England's Deposits were withdrawn, and also that ten millions of its Note-circulation were cashed,—the remaining assets of the establishment would then amount to forty-one millions, while its remaining liabilities would be only twenty-two millions. In other words, in such circumstances the Bank's Assets would be double the amount of its Liabilities,—instead of only one-half greater, as at present.

Nevertheless a withdrawal of deposits, if made suddenly and to a large extent, always produces embarrassment to a bank, and sometimes also loss. An unusual withdrawal of deposits compels a bank to convert a

portion of its reserve of securities into currency (that is to say, it must sell a portion of those securities); while the market at such times is usually much depressed,—so that the bank gets less than the ordinary price for the portion of its securities which it is forced to sell. Every bank in this country is liable to a loss of this kind in exceptional times, except the Bank of England. The Scotch and Irish banks, when an unusual demand for deposits is made upon them, have to cash their reserve of Government stock in order to provide themselves with more gold (not because they naturally require more gold for issue, but because, under the present system, they must get more gold before they are allowed to extend their note-issues). And the English banks, in like circumstances, have to sell a portion of their Government stock in order to provide themselves with more currency, in the form of Bank of England notes. But, be it observed, the Bank of England does nothing of the kind. If its gold be reduced, or its notes withdrawn, it takes no means to provide itself with either. If there be an unusual run upon it for deposits, the Bank takes no step to enable it to issue more notes; or, if the demand for deposits remain as usual, but more gold (instead of notes) is wanted in payment of them, the Bank equally takes no step to provide itself with gold. Thus, then, although a sudden withdrawal of deposits does generally cause a trifling loss to banks (but without diminishing the ratio of their surplus to their liabilities), such a loss is never incurred by the Bank of England. Its stock of currency, the means by which it must meet the demands of its depositors, may

decrease *ad libitum*, but never in any case (according to its present practice) does the Bank expose itself to loss in order to provide itself with more currency.

Yet there is one form in which loss occasionally arises to the Bank in connection with its Deposits,—not directly, it is true, but mediately—*i.e.*, through the operations by which the Bank makes use of (lends out) the money intrusted to its keeping.

The Loans and Discounts.

The Bank lends out at interest the money deposited with it, receiving in exchange commercial bills and other kinds of securities. Hence the amount of its loans and discounts (which is represented in its weekly returns by the amount of "other securities" which the Bank holds) in ordinary times very nearly corresponds with the amount of its Deposits—*i.e.*, about 20 millions. As a question of fact, it is upon this part of its business only that the Bank is liable to loss. If any of the bills or bonds prove of less value than the sum advanced upon them, then the Bank sustains a loss to that extent. To meet such losses is the only object of the Bank's reserves—*i.e.*, of its surplus of assets over liabilities. And this surplus, as already shown (even after setting aside 22 millions of its assets as security for its average Note-circulation), amounts to 19 millions,—wholly available to replace any loss caused by some of the bills and other securities, upon which it has lent out its Deposits, proving bad,—a reserve equal to 95 per cent on the amount of those liabilities.

As a matter of fact, there is no other bank which

does not regard 30 per cent as an amount of reserve ample for all contingencies.

COMPARISON WITH OTHER BANKS.

Let us take the case of other banks. And first, as to purely banking-liabilities—*i.e.*, apart from the liabilities connected with an issue of notes.

The London and Westminster Bank has an amount of banking-liabilities nearly equal to those of the Bank of England, yet it carries on business with a surplus of assets seldom exceeding four millions, — whereas, as above stated, the Bank of England's reserve in its Banking Department amounts to 19 millions. The Union Bank, with a similar amount of liabilities, keeps a somewhat smaller amount of surplus. And if we take the London joint-stock banks as a whole, we find that a surplus of 20 or 25 per cent of assets over liabilities enables them to carry on their business with perfect safety and great success.* Yet these banks are as liable to pay all their deposits back in money as the Bank of England is. It is true they cannot be called upon to

* It is true that the Bank of England is more liable than other banks to large withdrawals of Money; but this is simply in consequence of its holding (and having the use of) reserves of other banks. Moreover, this never occasions any loss to the Bank, because (as we have said above), unlike all the other banks, the Bank of England never takes any steps to provide itself with more money, whether in the form of gold or of notes. The only kind of loss, then, to which the Bank is liable, under the present system, arises from its Loans; and, owing to the select nature of the business which it carries on, its liability to loss from this source is even less than that of the other banks.

pay in gold,—for the notes of the Bank of England have been made a legal tender; but they must supply themselves with these notes just as the Bank of England can supply itself with gold. Each of those banks alike, when an unusual amount of deposits is called up, must supply itself with currency by realising some of its assets, or using a portion of the surplus which it keeps in the form of money. It costs a bank as much to get Bank of England notes as it does to get gold; hence the Bank of England, when called upon for more gold than it holds (if it were to meet the demand), would have to do no more than the other banks have to do when called upon for more notes. The only difference is, that the Bank of England can best get gold abroad,—it cannot readily get it here, for, when it sells a portion of its securities, it is paid in its own notes. But it can get gold abroad quite as cheaply as other banks can get money (whether notes or coin) at home.

Moreover, the liabilities of those banks consist entirely of Deposits; whereas one-half of the liabilities of the Bank of England consist of its Note-circulation, which is a much less onerous charge.

Next, take the case of the Bank of France,—the position of which establishment, alike as a bank of issue and as a quasi-Government bank, most nearly corresponds to that of the Bank of England. Let us compare the amount of the Assets held by those two great establishments with the amount of their Liabilities—*i.e.*, the extent of business which they carry on. The figures in the following table represent millions sterling: the position of the Bank of France is computed from the

average of the weekly returns in the twelve months of 1865,—the statistics for the Bank of England are given in accordance with our already-stated estimate of its condition in ordinary times:—

	Liabilities.		Assets.			Total.		
	Notes.	Deposits.	Gov. Sec.	Priv. Sec.	Specie.	Liabilities.	Assets.	Surplus.
Bank of England,	22	20	26	20	15	42	61	19
Bank of France,	33½	11	7⅓	26*	18	44½	51⅓	7

Thus it is seen that the Bank of France carries on business—and it does so most successfully—with an amount of assets not exceeding *one-sixth* of its liabilities; while the assets of the Bank of England are nearly *one-half* larger than its liabilities. Moreover the Bank of France is bound to let the Government draw upon it at any time to the extent of 2½ millions (£2,400,000), while the Bank of England is not liable to any similar demand. In fact, as appears from the preceding table, if the Bank of England kept a surplus of assets of only 7 millions (instead of 19), its position would seem as secure as that of the Bank of France. And yet the credit of the Bank of France is as undoubted as that of the Bank of England.

But there is an important point of difference in the circumstances of these two Banks. The Note-circulation of the Bank of France constitutes three-fourths of its total liabilities; whereas the Bank of England's Note-circulation constitutes only one-half of its liabilities,—

* We deduct from these Private Securities of the Bank of France £1,600,000,—this sum being lent upon bullion, which bullion is included in the Assets under the head of "Specie."

that is to say, is only equal in amount to its deposits. And—despite the current opinion to the contrary—it is the Deposits, and not the Notes, which are really the onerous portion of a bank's liabilities.* Hence the reserve-assets of the Bank of England ought to be (as it is) larger in proportion than those kept by the Bank of France.

Nevertheless, after making every allowance for this point of difference, the Bank of England's surplus of assets is too large for the amount of business which it carries on. Since the Bank of France, with fully 44 millions of liabilities, can meet all the wants of the public, and maintain its credit at the highest point, with a surplus of only $7\frac{1}{3}$ millions, it is obvious that 19 millions are a needlessly large surplus to be kept by the Bank of England, which has only an equal amount of liabilities.

The natural consequence of this difference in the practice of the two Banks is to be seen in the different rates of dividend which they pay. The ordinary amount of profits divided by the Bank of France is slightly more than £1,200,000 a-year; the ordinary profits of the Bank of England amount to slightly more than £1,300,000. Thus the profits of the two Banks are almost equal. But while the dividend of the Bank of England amounts on the average of years to 9 per cent, that of the Bank of France averages $16\frac{1}{2}$ per cent.†

In this exposition of the position of the Bank of England, we take note only of its liabilities to the public: its

* *Vide supra*, p. 151-52, and 162-63.

† The dividends paid by those two Banks during the last few years

liabilities to its shareholders being a private affair. But in order to render our exposition complete, we may state that the paid-up capital of the Bank amounts to £14,553,000; and in addition there is a large sum of undivided profits (called "the Rest"), which is never allowed to fall below £3,000,000, and which averages throughout the year £3,350,000. Thus, actually, the "proprietors' capital" of the Bank amounts to about 18 millions sterling,—nearly corresponding with the surplus of the Assets over Liabilities, which usually amounts (as above shown) to 19 millions.

These facts ought to put an end to the extraordinary complaint, vehemently made in some quarters, that the capital of the Bank of England is too small. This complaint is the offspring of ignorance. The origin of the complaint—which the complainants fail to see—is the mal-arrangement of the Assets of the Bank (partly due to the Bank Act, but partly also to the mistaken

were as follows (the Bank of England's dividends during 3 of those years (1864-5-6) having been unusually high):—

Bank of England.		Bank of France.	
1862 . .	8½ per cent.	1862 . .	15·8 per cent.
1863 . .	8¾ ,,	1863 . .	16·5 ,,
1864 . .	10¾ ,,	1864 . .	20 ,,
1865 . .	10⅓ ,,	1865 . .	15·4 ,,
1866 . .	11¾ ,,	1866 . .	15·6 ,,
1867 . .	10 ,,		

We may add that the Bank of France has a means of extending its accommodation to the public, and likewise of increasing its profits, simply by extending its note-issues, subject only to maintaining their convertibility; whereas the Bank of England at present has no such power. It cannot increase its note-issues without equally adding to its stock of gold in the Issue Office, whereby the profit on this business is nullified.

management of the Directors), whereby an enormous amount of the Bank's resources are virtually nullified, and can only come into use in the impossible case of the Bank's insolvency.

THE FORM IN WHICH ITS ASSETS ARE KEPT.

Next, putting into temporary abeyance this question as to the amount of the Bank's assets compared with its liabilities, let us proceed to the second stage of our inquiry, and see if this immense amount of wealth is kept in good form—*i. e.*, in the shape most available to meet either the actual or the possible demands upon the Bank.

The assets of the Bank are of three different kinds: namely, Government securities, coin and bullion, and private securities. Of the private securities we need not speak: they are of the same kind as with other banks. Therefore we need only concern ourselves with the two other kinds of assets,—namely, the Government securities, and the coin and bullion.

The Government securities are at present held partly in the Issue Department, partly in the Banking Department; 15 millions in the former, and about 11 millions in the latter.

Government Securities in Issue Department.

Let us consider, first, the Government Securities held in the Issue Department. These consist of 11 millions of Government Debt, and 4 millions of Government stock. The Debt, as we have said, was part of

the loans made to the Government by the Bank in order to obtain a continuance of its exclusive privileges. The loans were made, the Debt was created, not as a necessary means of securing either the notes or the general solvency of the establishment, but in order to preserve the monopoly first conferred upon the Bank in 1708. By the Act of 1844, the Debt was placed among the assets of the Issue Department, professedly as a security for the note-circulation. But this was an afterthought. The Bank never thought, or found it necessary, to secure its notes by such means. The credit of its notes had never been questioned. Moreover, the alteration thus made in 1844 was merely nominal. The Bank had not the power to part with any portion of the Debt: independently of the Act, the Debt must have remained as before, a fixed portion of the Bank's assets, until the Government was authorised by an Act of Parliament to pay it off. The Act of 1844 in no way made any addition to the assets or general solvency of the Bank : it simply decreed—with what wisdom we shall see—that this Debt, and 3 (now 4) millions of the Government stock held by the Bank, should be kept apart, locked up in the Issue Department. These Government securities were held by the Bank before, and, as regards the amount of the Debt at least, were then as available as security for the notes as they are now. Only, instead of the 11 millions being regarded as a debt which the Government ought to repay, this amount of securities was thenceforth said to be a basis for the Bank's notes which it was absolutely incumbent upon the Bank to keep.

The theory or principle upon which this arrangement was justified was this: It was said, "Experience shows that the amount of the Bank's note-circulation which never is or can be cashed is 14 millions; therefore no gold is needed to secure those notes." At the same time (as will be immediately shown) no *special* security was provided for this amount of notes at all. Why, then, was the Bank not left to use its own discretion in the matter? Why was this immense amount of assets withdrawn from its use and locked up in the Issue Department? Because (it was replied) it was the privileges conferred upon the Bank which enabled it to acquire so large a note-circulation; therefore the Bank should *pay* for this,—the State should get some advantage from the profitable result of the exclusive privileges which it had conferred upon the Bank. In literal fact, then, the cause of this Debt not being repaid, and of its being made a part of the fixed assets of the Bank, was substantially on the State's account. Just as it had been for years before. Only, instead of acknowledging, as previously, that this loan of 11 millions was a bonus advanced by the Bank for its monopoly, which ought to be repaid by the Government as soon as possible, in order that the banking-system of the country might be put upon a fair footing, it was said that the Debt ought to be continued as a new security for the Bank's note-issues. Nevertheless no such new security was established. The name of the thing was altered, but the position remained unchanged. The general solvency of the Bank was not strengthened, nor were those locked-up assets rendered any more available as security for the note-issues than before. Neither

the amount of the Debt nor the other Government securities locked up in the Issue Department are legally secured for the note-holders. The depositors have an equal claim upon them with the note-holders. If those assets were meant to be a special security for the notes, they ought to have been legally appropriated for that purpose; but they are not. Accordingly they are merely a portion of the general assets of the establishment which the Bank cannot use,—which are only available in the event of the insolvency of the Bank,—and which then can be claimed by the Depositors as well as by the Note-holders. They are simply a part of the immobilised reserve-wealth of the Bank.

The fact that the Bank's assets are of inordinate magnitude compared with the amount of business which the Bank can at present carry on—far exceeding not only the actual or probable but even all possible requirements of the establishment—renders it unnecessary for us to inquire whether the assets in the Issue Department are kept in the best or most available form. A Government Debt is a bad form of banking-reserve,—for it is not convertible into money, as Government Stock is: and a banking-reserve, if needed at all, ought to be kept in a form readily convertible into money. Nevertheless, as regards those eleven millions of Debt, it were a work of supererogation to discuss the question. Whether or not the Bank should be compelled to hold this amount of capital locked up in the Issue Department is a question of some importance; but if the Bank be compelled to do so, there can be no objection to the form in which those eleven millions are kept.

Government Securities in Banking Department.

A very different case presents itself for consideration when we come to the eleven millions of Government Securities ordinarily kept in the Banking Department. The reserve in the Banking Department is really the most important point of all. It is on the Banking Department that the great demands are made. The great drains on the establishment, whether for notes or gold, arise in connection with its purely banking business. They would occur as frequently, and to as great an extent as at present, if the Bank did not issue a single note of its own. They are caused by the customers of the Bank withdrawing their deposits (or, which is the same thing, the amount of the bills which the Bank discounts for them) whenever or from whatever cause the monetary requirements of the country increase. If money is wanted in an international form—*i.e.*, for payments abroad,—then the deposits are withdrawn in gold; if it is wanted for home-business only, then the amount is withdrawn chiefly in notes, but partly also in sovereigns as small change,—for payment of wages, &c. Whether the demand be for notes or for gold, the result, under the present constitution of the Bank, is the same. If the depositor calls for notes, the Bank's reserve of notes is correspondingly diminished; if he calls for gold, the Bank has to cancel notes in its banking-reserve to an equal amount. Hence in either case, under the present system, what is wanted by the Bank is more gold,—either to replace the gold withdrawn, or (if notes only are wanted) to enable it to replace the notes with-

drawn. Therefore the reserve of securities in the Banking Department ought to be kept in a form immediately convertible into gold,—or else into an additional issue of notes. But it is not so kept. It consists of Government securities, which may be sold or lent on the Stock Exchange, but for which, when so lent or sold, the Bank receives payment, not in gold, but in its own notes. Hence a reserve kept in this form is singularly inefficient. It cannot supply the Bank with gold; and it can only supply it with notes by taking these notes out of the hands of the public and of the other banks, which (in times of pressure) are already insufficiently supplied with them.

The only use which the Bank makes of the large amount of Government securities kept in the Banking Department, is to sell—or else to take short loans upon —a small portion of them. Let us see exactly the nature of this operation. The Bank, as we have said, gets in exchange no gold—only its own notes: and as at such times there is a greater demand for currency than usual, the notes which the Bank draws in from the public with one hand, it has to give out again with the other. The notes are not increased in number by this process: the only effect is, to take an amount of notes from the public and from the other banks, and to concentrate them in the Bank of England. What the latter gains, the former lose. The consequence is, that the other banks and the public, being further straitened for notes, go to the Bank for a fresh supply, and thereby draw out again the notes which the Bank had just drawn in. The effect of the process, therefore, is *nil*, or infinitesimal. As the

Bank gets loans upon these Government securities below the minimum rate which it charges for the notes when lent out again in discounts, it makes a gain on the transaction, and does not in any case suffer loss. A very slight economy of the currency is the most that can be effected: that is to say, some notes not absolutely needed by their holders (*i.e.*, the other banks and the public) may be turned to account by being drawn into the Bank. But this is a mere trifle at most, and does not exercise the slightest appreciable effect upon the course of a monetary crisis.

Thus we see that this large reserve of Government securities in the Banking Department is not a means of adding to the note-circulation; neither is it made a means of bringing gold into this country, or of lessening the export of gold. It is not used as a means of supplying the Bank with gold, nor can it be used as a means of supplying the Bank with more notes, when these are needed; yet to obtain this supply is the very thing wanted,—it is the grand object for which the Bank's reserve is, or ought to be, kept. What is especially needed is, that the reserve of Government securities in the Banking Department should be kept in a form readily convertible either into gold or into domestic currency. Taking our monetary system as it is (which requires that more gold shall be kept by the Bank when more notes are needed by the public), this reserve of securities should be kept in a form readily convertible into gold. How is this proceeding to be effected? It might be done to an infinitesimal extent by the Bank keeping a portfolio of first-class foreign bills; but much better

by keeping part of its banking-reserve of securities in the shape of foreign stock,—in the shape of Government securities held in those countries to which our drains of gold usually flow.

To keep a portfolio of foreign bills would have no more effect in supplying the Bank with gold than the cashing of its securities at home has in adding to its stock of notes: that is to say, the process might make a very slight economy of those foreign bills, but that is all. It could not increase the amount of foreign bills in this country,—*i.e.*, it would not give us any more means of making payments abroad without the use of specie. The foreign bills kept by the Bank would be just so many withdrawn from the portfolios of the merchants. If the Bank were, in times of difficulty, to buy up foreign bills *abroad*—as the Bank of France has done on several occasions,—the effect would be much more important; but merely to keep a portfolio of foreign bills, drawn from the keeping of our own merchants, would be of no appreciable use.

The purchase of foreign bills abroad would be an exceptional transaction suited (if there were no better plan) to meet exceptional and transient emergencies. But even to facilitate such a course, the reserve of securities in the Banking Department ought to be kept in a form different from what it is at present. What is really required is, that the Bank should keep a portion of its reserve of Government securities in the shape of Government stock abroad,—in those countries to which our drains of specie usually flow. By selling or taking loans upon that stock, the Bank could either draw specie

to this country, or lessen our exports of gold by giving to its customers drafts upon foreign banks—upon the banks of the country to which it is necessary to send specie. This process would give what is so often wanted,—namely, a means of adding to our stock of international currency, and thereby of lessening our export of gold in times of foreign drains. This is a point which will be fully discussed in the sequel.

Bullion in Issue Department.

In addition to the 15 millions of Government securities (of which we have already spoken), the Issue Department holds on the average nearly 15 millions of coin and bullion. The great fact to be noted, as regards this stock of coin and bullion, is that one-half of it is practically nullified. One-half of it is of no use whatever in carrying on the business of the Bank, however urgent may be the exigencies of the establishment: it counts for nothing, and can only become available in the event of the Bank becoming insolvent. Fully seven millions of the reserve of coin and bullion are *de facto* as useless as if they were kept buried by Act of Parliament beneath the solid foundations of the Bank. The Bank might possibly, in some great emergency, sell or mortgage the buildings in which it carries on its business, but it cannot possibly touch or pledge any part of those seven millions of gold. Not a particle of that large amount of specie can be used even to ward off bankruptcy. A few words will serve to explain how this strange result is produced:*—

* The following statement is condensed from my work on the

For every note issued beyond the arbitrarily fixed sum of £15,000,000, the Act of 1844 requires that the Bank shall hold a corresponding amount of gold. As the ordinary amount of notes required for the wants of the public is £22,000,000, it follows that £7,000,000 is the lowest amount of gold that must be in the Issue Department to allow of those 22 millions of notes being kept in circulation. And taking into account the requirements of the branches of the Bank and other matters, this sum may safely be stated in round numbers at fully 7½ millions. As a matter of fact, when the gold in the Bank falls to this amount, the Bank Act has to be suspended.

Thus, when fully 7 millions of specie are in its possession, and 22 millions of notes are in circulation, all the notes which the Bank is allowed to issue are in the hands of the public. When this point is reached—when the bullion in its possession has sunk to this level,—the Bank cannot issue a single additional note. Neither can it part with a single gold-coin. As discounted bills fall due, the Bank may discount others to an equal amount; but that is the most it can do. However pressing be the emergency, the Bank cannot extend its banking-accommodation one iota. What is more, when an actual crisis arrives, it cannot even continue it. Its Issue Department being literally shut up, it must withdraw from its discount-business whatever amount of notes may be called for by its depositors. Otherwise, if a depositor were to ask at such a time for even a

Economy of Capital, where the disastrous working of this provision of the Act of 1844 was fully pointed out.

£5-note, the Bank could not give it,—its legal power to issue notes being exhausted. And if the depositor were to say, 'Then give me the sum in gold, of which you say you have fully 7 millions,' the Bank must reply that this form of issue is shut up too, because every sovereign of those 7 millions is needed in its own vaults in order to avoid an infringement of its Charter. Thus the Bank at such times cannot make payment of a single note or sovereign to any of its depositors, except by withdrawing a similar amount from its loans and discount-operations, which are the mainstay of trade and credit. And this artificial dilemma occurs at times when, as every one knows, there is a greatly increased demand for loans and discounts at the Bank of England, owing to the increase in the monetary requirements of the community which always takes place in times of crisis.

The effect of this arrangement is, that one-half of the average stock of gold held by the Bank is of no use—cannot in any way be employed in carrying on the business of the establishment. It is highly important to observe the practical consequences of this arrangement as regards the community. This artificial curtailment of the resources of the Bank renders monetary crises more frequent and more disastrous than ever. Fully 7 millions of gold being nullified, when the bullion in the Bank falls to 9 millions, a crisis ensues as violent as used to be when the specie was reduced to 1 or 2 millions. The Bank has to stop when it still has fully seven millions of gold, just as if the gold had fallen to zero. Thus every trifling ebb of specie from

the Bank is, under the present system, converted into a serious national disaster.*

What is more, the effect of this arrangement weighs upon the community at all times. Not only, at recurrent periods, does it produce great monetary crises, but it permanently and artificially enhances the rate of discount throughout the whole country. The Bank Directors now regard seven millions of their stock of specie as non-existent. When they have fourteen millions of gold, they act as if they had only seven. Seven millions form the zero-point in their calculations: that is to say, one-half of the ordinary amount of bullion in the Bank is nullified, and a double price is charged for the other half. It is needless to say that the special interest of the Bank Directors, and of the directors of all banks, is to keep the rate of discount as high as possible. It is

* As shown in November 1857, the Bank has to fail, or the Bank Act has to be suspended, when there is £7,170,000 of coin and bullion in the establishment. Consider for a moment the magnitude of this waste. This amount is nearly equal to the whole stock of specie (£8,000,000) which the Bank held, on the average, for the twenty-five years previous to the passing of the Bank Act—namely, from 1819 to 1844. Or look at the case of the Bank of France. That Bank, with a note-circulation fully one-half larger than that of the Bank of England, and whose loans to the public are likewise much larger, has often carried on its usual amount of operations with only seven millions of specie. During December 1863 and January 1864, its stock of specie averaged exactly seven millions sterling; and for several months at that time, the Bank of France, with equal liabilities to those of the Bank of England, had only half as much specie, and yet charged less for its loans; while more confidence prevailed in the commercial world of France than in ours. Finally, to show the true value of the specie thus wasted, nullified, by the Bank Act, we may state that seven millions of gold much more than suffices for the wants of all the Scotch and Irish banks put together, although the liabilities of those banks are nearly treble those of the Bank of England.

as natural for bankers to desire to keep up the price of money on loan as it is for farmers to wish for high prices for corn. Bankers will always keep the rate of discount as high as they possibly can. But in the present case the Government imposes a useless burden upon the Bank, which the Bank naturally seeks to shift on to the shoulders of the community. When the amount of bullion in the Bank is between thirteen and fourteen millions, the rate of discount is frequently raised to 8 or 10 per cent. For example, in December 1863, when the minimum Bank-rate was 8 per cent, the stock of bullion averaged $13\frac{1}{3}$ millions. And in the autumn of 1864, the Bank-rate stood for two months at 9 per cent, while its amount of gold averaged nearly $13\frac{1}{4}$ millions. Again, in May, June, and July 1866, the Bank-rate was 10 per cent, although its stock of gold averaged upwards of $13\frac{1}{2}$ millions.

Having thus reviewed the position of the Bank as it is, let us recapitulate. The three great points which come into view are: 1. That the assets of the Bank are inordinately large in proportion to the amount of business which, under its present restrictions, the Bank carries on. 2. That the reserve of Government securities in the Banking Department is kept in a useless form, and is never employed (as such a reserve ought to be) to procure gold for the Bank when gold is needed. 3. That nearly one-half of the ordinary amount of gold held by the Bank is practically useless — cannot be employed at all in the business of the Bank, —constituting a dead loss to the establishment, which

the Directors naturally seek to shift on to the shoulders of the public.

One effect of the burdens and restrictions placed on the Bank by the Government—and still more of the virtual monopoly possessed by the Bank—is to be seen in the misuse which the Directors make of the Government securities in the Banking Department. They never employ these assets as a means of getting gold. Instead of taking steps to supply themselves with gold when more gold is needed, the Directors prefer to charge a double or a treble rate for all their money, whether gold or notes. Thus the Bank makes use of its privileges to nullify its burdens.

THE NEW SYSTEM.

The remedy to be applied is as obvious as the existing defects. In brief, we must lighten the burdens upon the Bank, and at the same time abolish its monopoly. We must put an end to the present waste of the resources of the Bank, by rendering them as available as is possible to meet the requirements of the establishment. Especially, in so doing, we must raise the embargo upon the seven millions of gold (at present locked up passively in the Issue Department), which ought to be the most effective portion of the Bank's reserve. This embargo is a serious tax upon the Bank (seeing that this gold bears no interest), and also is one cause of the exorbitant raising of the Bank-rate which has of late become so frequent and so disastrous to the trade and industry of the country.

It were useless to attempt to deal with the position of the Bank as if it presented a *tabula rasa*. We must pay deference to existing, and long-existing, conditions. Hence our object is to effect a maximum of improvement with a minimum of change. The reserve-wealth of the Bank (*i. e.*, the surplus of its assets over its liabilities) is unquestionably larger than is actually needed: but we do not propose to lessen it. We would use it as a means of greatly extending the Bank's business. Instead of lessening the capital, we would let the Bank's business work up to it. Moreover, the present magnitude of its reserve-wealth affords a means of basing the note-issues of the Bank upon the principle which we have proposed to apply to the general monetary system of the country, without imposing any burden upon the Bank in lieu of those from which we think it ought to be freed.

The first and greatest reform which we propose is this:—Let the note-issues of the Bank be fully covered by a corresponding amount of Government securities, legally secured for the note-holders: thereafter let the other assets of the Bank be freely at the disposal of the Directors,—to be used in whatever way the interests of the Bank may require. This will preserve in essence the separation between the Issue and the Banking Departments of the establishment, without the embarrassments produced by the present constitution of those departments. Under this new system, fully seven millions of gold, yielding no interest, would be withdrawn from their present condition of passivity, as a *vague* security for the notes, and would be replaced by an equal

amount of Government securities, yielding interest to the Bank, and *expressly set apart for the note-holders.*

With those changes made, let us see what would be the constitution of the Bank of England. Taking the ordinary position of the Bank (as we have hitherto done) as a basis—that is to say, with 22 millions of notes, 20 of deposits, 15 of specie, 26 of Government securities, and 20 of private securities,—the position of the establishment would be as follows. The figures in the table represent millions sterling :—

NEW SYSTEM.

LIABILITIES.		ASSETS.			
Notes.	Deposits.	Security for Notes.		General Reserve.	
22	20	The Debt, . . 11 Government Securities, . . 11	22	Gold, . . . 15 Gov. Securities, 4 Private do., . 20	39
42			61		

Or the same position may be exhibited in this way :—

LIABILITIES.		ASSETS.				
Notes.	Deposits.	Security for Notes.		Security for Deposits.		Reserve.
22	20	The Debt, 11 Government Securities, 11	22	Bills and other Private Securities, . .	20	Gold, 15 Gov. Sec., 4 — 19
42			61			

The most important result of these changes, as is obvious, is greatly to add to the effective strength of the Bank's Reserve. The amount of the Bank's assets kept in reserve remains the same, but the amount of that reserve which exists in an effective form is largely increased. A great and most important addition is made

to the portion of the reserved assets which consists of Money. At present the Reserve in the Banking Department consists on the average of 11 millions of Government securities and (say) 8 millions of notes; whereas under the new system it would consist of 4 millions of readily convertible stock (Consols and Exchequer bills), and 15 millions of gold.

But the effects of the New System would go much further than this. The whole amount of the reserved assets would become available. This would remedy one of the most striking defects of the existing system. At present, when the notes and coin in the Banking Department fall to 5 millions (whether from a demand solely for notes, or for gold alone, or, as a foreign drain often produces an internal one also, for notes and gold simultaneously), there are also in the Banking Department about 11 millions of Government securities,—making the total Banking Reserve amount to 16 millions. How, then, is it that embarrassment arises at such times? Because *two-thirds of the Banking Reserve are at present useless.* The Government securities in the Banking Department cannot be converted into currency (notes) save by withdrawing an equal amount of notes from the public and the other banks. The monetary requirements of the public remaining as before, the notes thus acquired by the Bank are immediately drawn out again by the other banks and by its private customers. Hence the Bank's present practice of taking loans upon a portion of its Consols, though profitable to the establishment, is quite illusory as a means of adding to its reserve of money. The present consti-

tution of the Banking Reserve is perfectly absurd; it is also a waste of resources, for which the community suffers. Even in ordinary times—*i.e.*, when there are eight or nine millions of notes and coin in the Banking Department—the useless portion of the Banking Reserve exceeds one-half of the whole amount. When the notes and coin fall to five millions, nearly three-fourths of this Reserve are useless. And when all the notes and coin are used up, the whole of the Reserve (still consisting of eleven millions in the form of Government securities) is as useless as if it were non-existent! It is a mirage, which becomes "nowhere" when approached.

Under the New System the case would be very different. The Government securities held in the Banking Department would be immediately convertible into an equal amount of bank-notes. By transferring a portion of those securities into what may still be called the Issue Department (although this would be made a Government office), the Bank would be entitled to issue additional notes to a like amount. So that, at any moment, the Bank could transmute the Government securities in its banking-reserve into an equal amount of currency in the shape of notes. The gold in the banking-reserve, of course, would be likewise transmutable into notes. If the demand were for notes, the Bank would either take some of its Consols from the banking-reserve, or would purchase such stock with its gold, and, depositing these Consols in the Issue Office, would receive in return an equal amount of notes. In this way the whole of the Banking Reserve, alike the Government securities and the gold, would be rendered

available to meet the requirements of the establishment. What would be the result? The effective resources of the Bank would in ordinary times be fully *doubled,* and in times of difficulty *trebled* or *quadrupled.*

The portion of the Reserve consisting of Consols would not be of any use in procuring for the Bank a supply of gold. The gold could be converted into Consols and the Consols into notes, but the Consols could not be converted into gold,—because the Bank might be paid in its own notes whenever it sold any portion of its securities. Accordingly the proportion of gold in the Reserve should greatly exceed that of Consols. The largest amount of *Consols* held in the banking-reserve should not be more than sufficient to meet the possible requirement for *Notes.* When the note-circulation stands at 22 millions, the portion of the Reserve consisting of Consols should not exceed 4 millions,—26 millions being the highest point which the note-circulation has reached. In the ordinary position of the Bank (viz., with 22 millions of notes, 15 of gold, and 19 of Reserve in the Banking Department) this would leave 15 millions of the banking Reserve in the form of gold. In similar circumstances, under the present system, the amount of cash in the Banking Reserve is only 8 millions. And after setting aside half a million of gold for the cashing of notes (which is about ten times the amount usually needed), the amount of the Reserve available for purely banking-purposes (viz., 14½ millions of gold and 4 millions of Consols, convertible into notes) would be more than twice as large under the new system as under the present one.

In fact, in the ordinary position of the Bank under the New System, several millions of its gold might with perfect safety to the public, and obviously with profit to the Bank, be invested in Government stock abroad. When a demand for gold for export arose, the Bank would take short loans on those foreign securities, and give drafts for the amount to its customers; so that the gold in Bank would not be touched until those foreign securities, or the greater part of them, had been turned to account—reconverted into gold. Such a process would be more profitable to the Bank than keeping its whole stock (at present amounting to 24 millions) of gold in hand; and at the same time the Bank's power of supplying its customers with gold would be as great as at present. Say that the Bank should, in ordinary circumstances, keep 10 millions of gold: this, in addition to the 4 millions of Consols convertible into notes, would make the effective Reserve in the Banking Department amount to 14 millions, while in addition the Bank would hold 5 millions of foreign stock convertible into gold when required. This is taking the average position of the Bank,—as we do throughout. Of course, when its stock of gold increased beyond the average amount, there would be so many more millions to invest in foreign securities,—with a corresponding addition to the profits of the Bank.

To bring clearly into view the bearing of the New System, as compared with the present one, let us show what will be the variations in the amount and form of the *Reserve* under several different positions of the Bank. First, let us suppose that the note-circulation

remains at its ordinary amount, while the Bank's stock of gold varies from a minimum to a maximum :—

NOTE-CIRCULATION = 22 MILLIONS.

GOLD = 7 MILLIONS.		GOLD = 20 MILLIONS.		
Position of the Banking Reserve.				
At Present.	As Proposed.	At Present.	Proposed Alternatives.	
			either	*or*
Govt. Secs., 11	Govt. Secs. *convertible*, 4	Govt. Secs., 11	Govt. Secs., 4	Govt. Secs., 4
Notes & Coin,* 0	Gold & Coin, 7	Notes & Coin, 13	Gold & Coin, 20	Gold & Coin, 10 Foreign Stock, 10
Millions, 11	11	Millions, 24	24	24

Next let us vary the case, and suppose that the Gold remains at its ordinary amount (say 15 millions), while the Note-circulation varies :—

GOLD = 15 MILLIONS.

NOTE-CIRCULATION = 19 MILLIONS.		NOTE-CIRCULATION = 25 MILLIONS.	
Position of the Banking Reserve.			
At Present.	As Proposed.	At Present.	As Proposed.
Govt. Securities, 11	Govt. Secs. *convertible*, 7	Govt. Securities, 11	Govt. Secs. *convertible*, 1
Notes and Coin, 11	Gold & Coin, 15	Notes and Coin, 5	Gold & Coin, 15
Millions, 22	22	Millions, 16	16

Or, let us suppose that the gold in the Bank of England runs down to 9 millions, while the requirements of the public keep the note-circulation at 23 millions. Under the present system, the Bank, in such a case, must stop; whereas, under the New System, the banking

* In this case the Bank Act must be suspended, for the Bank is no longer able to carry on business when its Banking Reserve of notes and coin falls to £1,000,000.

Reserve would actually be in a much better position than it occupies in ordinary times under the present regime:—

NOTES = 23 MILLIONS. GOLD = 9 MILLIONS.

Position of the Banking Reserve.

At Present.		As Proposed.	
Government Securities, .	11	Government Securities (*Convertible into Notes*),	3
Notes and Coin, . .	1	Gold and Coin, . .	9
Millions,	12	Millions,	12

Finally, fully to test the resources of the New System, let us suppose that the gold in the Bank falls to 7 millions, while, owing to extraordinary circumstances, the note-circulation stands at 25 millions. Even then the banking Reserve under the New System would be little less than the effective portion of it (the notes and coin) is in ordinary circumstances under the present system; and the amount of gold would be fully equal to that with which the Bank of France at times carries on its whole business without disquiet or embarrassment. The Reserve would, in this very exceptional case, stand thus:—

NOTE-CIRCULATION = 25 MILLIONS. GOLD = 7 MILLIONS.

The Banking Reserve.

Government Securities, . . .	1
Gold,*	7
Millions,	8

* In a case like this (if such were to happen) the Bank would not be likely to convert any of its gold into Consols or notes.

The two features of the New System are: 1. A re-distribution or re-arrangement of the assets of the Bank, so as to economise the Bank's resources by placing each item of its assets in the place where it will have a maximum of efficiency. 2. The power to increase the issue of notes, when required, upon the Bank depositing in the Issue Office a corresponding amount of Consols. Let us consider the effect of each of those changes separately.

I. The Re-arrangement of the Assets of the Bank.—Taking the note-circulation at its ordinary amount (22 millions), the 26 millions of Government securities at present held by the Bank would be disposed of thus—22 millions deposited in the Issue Office, and 4 millions in the Banking Reserve. If the note-circulation increased, the Consols in the Reserve would be correspondingly diminished; if the circulation fell, a correspondingly greater amount of Consols would be added to the Reserve. As regards the Gold (which in ordinary times amounts to about 15 millions), the whole of it would be placed in the Bank's Reserve,—to be employed alike in the cashing of notes, and for the specie-payments required by depositors or discount-customers. The effect of this arrangement, as we have fully shown, would be in ordinary times to double, and in times of difficulty to treble or quadruple, the effective or really available portion of the Bank's Reserve. For example (quite independently of the second part of our scheme, *i.e.*, the power to issue notes on the deposit of Consols), the difference between the present and the proposed

systems, during a heavy drain of gold, would be this:—

NOTE-CIRCULATION = 22 MILLIONS. GOLD = 7 MILLIONS.

State of the Banking Reserve.

PRESENT SYSTEM.		NEW SYSTEM.	
Government Securities, .	11	Government Securities, .	4
Notes and Coin, . .	0	Gold and Coin, . . .	7
Millions,	11	Millions,	11

When so circumstanced, under the present system, the Bank of England must stop; whereas, under the new arrangement of its assets (and apart from the power to issue notes on the deposit of Consols), the available portion of the Bank's Reserve would be nearly equal to its ordinary amount under the present regime. This important change would be effected simply by withdrawing seven millions of gold from the Issue Department (where at present they are locked up passively when the note-circulation is at its ordinary amount), depositing in their stead an equal amount of Government securities, and placing these 7 millions of gold in the general Reserve of the establishment.

It was purely by a mistake on the part of the framers of the Bank Act that this large amount of gold was thus locked up. In 1844 the current notion was that our drains of the precious metals were owing to the note-issues being redundant and depreciated, and that the drafts for gold upon the Bank were made by the note-holders, who, finding the notes depreciated,

took them to the Bank to be cashed. Every one now knows that this notion is utterly absurd. It has not an atom of foundation. As we have stated, the only cashing of notes which takes place is with a view to obtain "small change;" and even this demand would disappear if an issue of £1-notes were permitted. Indeed, it will surprise the public to learn that £50,000 in sovereigns is the full average amount required in the Issue Office for the cashing of notes. This is the fact.* And a fact more fatal to the principle, and more condemnatory of the details of the Bank Act, it is impossible to conceive.

* The number of notes paid into the Bank during the years 1841-59 (as given in the Parliamentary Return of 27th February 1861, p. 14) was as follows :—

AVERAGE NUMBER PER DAY.

1841, . . .	17,124	1851, . . .	24,816
1842, . . .	18,462	1852, . . .	26,340
1843, . . .	19,136	1853, . . .	28,417
1844, . . .	21,466	1854, . . .	28,209
1845, . . .	23,155	1855, . . .	28,698
1846, . . .	23,751	1856, . . .	30,234
1847, . . .	25,035	1857, . . .	31,148
1848, . . .	23,717	1858, . . .	30,666
1849, . . .	23,320	1859, . . .	32,098
1850, . . .	23,543		

If we take these notes at the average value of £20 each, and make allowance for the steady increase in their amount (*i.e.*, take their daily number at 50,000 at present), this would show £1,000,000 in notes daily paid into the Bank. So that, even if every one of those notes were paid into the Bank through the Issue Office, a million sterling would suffice for all the requirements of that department. But, in point of fact, only a very small fraction of this amount of notes is returned to the Bank in this way (*i.e.*, for the purpose of being cashed); by far the larger portion being paid into the Banking Department, as Deposits, or in repayment of the Bank's loans and discounts.

The Bank of England needs about 750,000 sovereigns as small change for its customers in the Banking Department; but it only needs about a twentieth part of that sum for the cashing of notes in the Issue Department. The whole of the large drafts for gold upon the Bank are made through its Banking Department: they are caused by depositors or discount-customers withdrawing their money in the shape of coin or bullion. But here we show that, even as regards the demand for gold as small change, the whole average amount of such demands, in both departments, is only three-quarters of a million; and, save a few thousands, the whole of that sum is needed in the Banking Department. Thus the new arrangement which we propose, by which all the gold will be taken from the Issue Department and placed in the general Reserve of the Bank, is strictly in accordance with the actual requirements of the case. The cashing of notes (a petty affair, requiring only a few thousands in coin) may be carried on in the same room of the Bank as at present, but simply as part of the ordinary banking business,—just as in the Scotch and Irish banks, and as used to be in every English bank prior to 1833, when the notes of the Bank were made a legal tender throughout England and Wales.

These advantages, we repeat, would flow from the New System simply from the re-arrangement which it makes of the Assets of the Bank.

II. The Power to issue Notes on Deposit of Consols. —Such a measure is necessary to impart to the currency that elasticity which is indispensable to meet the

varying monetary requirements of the country. We have fully discussed this part of the subject in the previous chapter. And in this chapter we have amply shown the efficiency of the New System to meet this requirement, and thereby remedy the defects of our present monetary system.

In fine, the great feature of the New System is to establish a re-arrangement of the assets of the Bank in such a way as immensely to add to their efficiency or active power, without altering the amount of the securities and assets with which the Bank carries on its business. And at the same time to render the whole (instead of merely a part) of the Government securities available as a basis of note-issues; so as to enable the Bank easily to meet an increase in the monetary requirements of the community,—subject only, as at present, to the convertibility of the notes into coin on demand. For the sake of clearness, we shall finally place the two systems side by side: taking the note-circulation at 22 millions,—the specie at 15 millions (of which £750,000 are at present kept in the Banking Department),—and the Government securities kept under the present system in the Banking Department at 11 millions:—

PRESENT SYSTEM.

Issue Department.		*Banking Department.*	
Bullion,	£14,250,000	Notes,	£7,250,000
		Coin,	750,000
Government securities,	15,000,000	Government securities,	11,000,000

NEW SYSTEM.

Government securities, (equal to amount of note-circulation.)	£22,000,000	Bullion and Coin,	£15,000,000
		Government securities, *convertible into Notes.*	4,000,000

The Government Debt to the Bank.

The immediate result, the necessary concomitant, of the establishment of the New System, would be the disappearance of the debt of eleven millions which the State at present owes to the Bank. The Government would take power to convert the Debt into Consols, which it would hand to the Bank in payment of the Debt; and the Bank would simultaneously deposit these Consols with the Government as a necessary part of the security for its note-issues. The Bank would receive from the Government the same amount of interest on these Consols as it at present receives for the Debt; but the nature of the relation between the Bank and the State would be changed. "The Debt" would be at an end. Thereafter the Bank would have no more claim upon the State than any private fundholder has.

This result, as will be observed, arises naturally and necessarily under the New System; for as, under the proposed system, the note-issues of the Bank (in common with those of all the other banks) are to be secured by an equal amount of Consols, the eleven millions at present represented by the Debt will be needed, in the form of Consols, to maintain the present issuing power of the Bank. The disappearance of the Debt, thus occasioned—although financially the change will produce neither gain nor loss either to the Bank or to the Government—is a matter of much importance politically. For, according to the Act of 1844, no alteration can be made in the privileges of the Bank except (upon twelve months' notice being given, and) on *repayment of all*

debts due from the State. This unusual condition—never before inserted in any renewal of the Bank's charter—created a formidable difficulty in the way of future legislation in regard either to the Bank itself, or to the bank-issues of the country at large. It is true that Parliament may assume the power to rescind this clause in the Act of 1844, and thereafter to reopen the whole question unconditionally. And, a few years ago, Parliament did not hesitate to use its powers in this fashion in a case of much greater importance, and of more delicacy, than that which we are at present considering.* Nevertheless, such a course of procedure is only justifiable in a case of necessity. And hence a great practical advantage arises from the New System in this respect, inasmuch as it removes the present obstacle to legislation, and allows Parliament to act freely and at once, in the interests of all parties, by reforming the banking and monetary system of the country.

NOTE.

I. Throughout this chapter, for the sake of simplicity, we have shown the effects of the New System upon the Bank of England in its present position,—*i.e.*, on the supposition that the amount and character of its business will remain unchanged. In the next chapter, we shall consider the changes likely to take place in the

* We allude to the case of the Loan Act, passed during the Russian war, which contained a stipulation that the Loan should be gradually extinguished by means of a sinking-fund,—a stipulation which Parliament subsequently annulled.

amount of its Deposits and Note-circulation,—in order to show the probable effects of the New System upon the *profits* of the Bank.

II. Also, throughout this chapter, we have treated the question on the supposition that the Bank be allowed to issue notes upon the basis of an exactly equal amount of Government securities, valued at the current market-price (deposited, as we have said, in a State Office, and kept specially appropriated for the note-holders in the event of the Bank's insolvency—*i. e.*, in the event of the Bank's being at any time unable to pay either its note-holders or its depositors in gold on demand). As the British Funds are the steadiest in value of all existing securities, this condition of issue is really all that is practically needed.

If the banks were compelled to deposit an amount of Consols somewhat greater in value than the notes which they receive in exchange from the Government Office of Issue, the object of this stipulation would be to prevent those deposited securities from falling below the full value of the notes issued upon them, in consequence of a sudden fall in the value of the Funds. But, it is to be noted that the banks, for their own convenience, would always keep an amount of Consols in the Government Issue-Office somewhat larger than the notes which they took from it. The banks would do so alike to save themselves trouble in connection with the small daily fluctuations in the price of Consols, and also in order to be at all times able to meet an increased demand for their notes. Hence, as a matter of fact, the deposit of an equal amount of Consols, valued at the current price,

would be a perfectly adequate condition of issue (*plus* the convertibility of the notes) for the banks of this country.

Nevertheless, as a theoretic precaution, and in order to obviate all possibility of sensitiveness on the part of the note-holders (*i. e.*, the public), or any portion of them, it might be stipulated that the issue of notes should be safeguarded by the deposit in the Government Office of an amount of Consols slightly greater in current value than the notes issued. (These deposited Consols, of course, only to be paid to the note-holders in the event of a bank's insolvency ; and then only to the exact value of other notes or gold-coin as measured by the current price of Consols,—any surplus of deposited Consols thereafter becoming part of the general assets of the insolvent bank.) In ordinary circumstances, this arrangement would suffice to give the banks 3 per cent interest on the Consols deposited in the Government Office as a basis of their note-issues.

XXII.

BANKING-PROFITS UNDER THE NEW SYSTEM

In all projects of reform, advanced not merely theoretically, but as a basis of practical legislation, it is important to consider the effects of the New System upon the profits of the establishments which will be affected by it. If the New System be calculated greatly to lessen the profits of those establishments, it will arouse an amount of opposition which may prove fatal to the adoption, or at least to the immediate adoption, of the proposed scheme. The plan of Monetary Reform which we have described is free from this difficulty. While securing the rights and promoting the interests of the community at large, it is at the same time in substantial accordance with the interests of the banks.

Let us examine this important matter in detail. And, first, let us take the case of

THE BANK OF ENGLAND.

At present, the charges upon the Bank of England consist of £120,000 for its Charter,—£60,000 as composition to the Stamp Office upon its note-issues,—and the profit upon one million of its note-circulation.*

The composition on the Bank's note-issues is simply a fiscal arrangement, which the New System would not affect. It is a tax which under the New System (as substantially at present) the Bank would bear in common with all the other banks of issue in the kingdom.† There remains the payment for its Charter, and also the payment to the State of the profit upon one million of its note-circulation. These are matters which open up a very wide and important question.

The peculiar privileges so long enjoyed by the Bank of England have enabled it to acquire a dominant posi-

* The portion of its notes upon which the Bank has to pay the profits to the State may be described as the 15th million of its circulation. By the Act of 1844, the Bank was allowed to issue 14 millions of its note-circulation upon an equal amount of Government securities: but it was stipulated that if (under certain circumstances specified) the Bank should be allowed to issue more than this amount of notes against Government securities, the profit on these notes should be paid to the State. At present the Bank is allowed to issue 15 millions of its note-circulation upon Government securities: so that the profit upon 1 million of its notes is now paid to the State. The profit on these notes is calculated by the current Bank-rate, minus the cost of paper and printing of the notes and the management-expenses connected with this portion of the Bank's circulation.

† Taking the Bank's note-circulation at 22 millions, the £60,000 which it pays as stamp-duty on its notes is a rate only very slightly lower than that which is paid by the other banks of issue,—namely, 7s. per £100, or rather more than ⅓ per cent.

tion over all the other banks of the country,—thereby conferring upon it a power over the currency, and consequently over the rate of discount, which the Bank would not otherwise have possessed. Under the New System, those special privileges will be abolished. Nevertheless, after the present system of monopoly is superseded, it is unquestionable that the Bank of England will still possess a dominating influence over all the other banks, and consequently over the rate of discount. It will remain by far the greatest bank of issue, the chief fountain of currency. And if it chooses to charge high rates for the use of its notes, all the other banks will still have a temptation to follow its example. For no bank willingly lends its money cheaply: every bank has a direct motive to keep the rate of discount as high as possible.

Hence the question arises,—Ought the State to make the Bank *pay* for the virtual monopoly which it has acquired, and which under any system it will long maintain?—and if so, in what form ought this State-charge upon the Bank to be made? What, in effect, should be done in regard to the charge which the State at present exacts from the Bank as payment for its Charter; and also in regard to the appropriation by the State of the entire profit upon a portion (1 million) of the Bank's note-circulation?

Both of those charges, we do not hesitate to say, are wholly vicious in principle; and, in practice, they are eminently unfavourable to the community. The prevalent idea of making a bank-of-issue pay for its monopoly, as a corrective of the evil effects of such a

monopoly, is most preposterous and illusive. So far from counteracting or even palliating the evils of the monopoly, this system most disastrously aggravates them. The privileged banks naturally make use of their monopoly to nullify the State-charges imposed upon them, by shifting the burden on to the shoulders of the community; and, as we have shown, the burden, when so shifted, falls upon the public with twentyfold severity.* There is but one way in which the State can intervene to palliate the effects of a monopoly (whether legal or *de facto*) of banking-currency: and that is, by preventing the privileged bank or banks from raising the rate of discount to an exorbitant point for the sake of adding to their profits,—*i. e.*, by enacting that, whenever the rate is raised above a certain point, the extra profits thus accruing to the privileged banks shall be at the disposal of the State. This is the principle which is adopted in France, and which more recently and more stringently has been adopted, after ample discussion, in Belgium. The Banks of France and Belgium are allowed to raise the rate of discount to any point they may find necessary to free them from banking-embarrassments, but they are not allowed to convert their seasons of difficulty into a source of additional profits to their shareholders.†

This is the right way to deal with establishments which possess a monopoly of the note-currency. But any State-interference of this kind will be unnecessary under the new system which we propose. In course of time, under a free system of banking, it may be expected,

* *Vide supra*, pp. 303-5. † Ib. pp. 286, 290.

as certainly it is to be hoped, that some of the other banks will gradually develop themselves to such an extent that, although each of them be still inferior in power to the Bank of England, yet their collective action will even in exceptional times (as during a crisis) form an effective check upon any undue exorbitance in the Bank's charges. Perfect freedom is the right course; and we would rather temporarily incur the risk of occasional exorbitance of charges on the part of the Bank, and trust to a check growing up in the future, than seek in any way to interfere by legislative enactments with the Bank's freedom of action. In any case, the system of what is called "making the Bank *pay*" for its privileges — by requiring an annual payment for its Charter, and also by the State appropriating the profit on a portion of the Bank's note-issues (except, of course, in the way of ordinary taxation)—ought certainly to be abolished.

Preliminary Changes.

The New System would at once abolish all the special State-charges upon the Bank of England,—at present amounting to about £136,000 a-year: namely, £120,000 for its Charter, and fully £16,000 as the profit upon a million of its note-circulation.*

* In the year 1860, the share of profits on its note-circulation which the Bank paid to the State was £8078 (*vide* Parliamentary Return, dated 7th February 1861). At that time the portion of Bank's note-circulation upon which the profit was paid to the State was £475,000; at present it is £1,000,000. So that the sum now paid to the State (although, of course, it varies from year to year with the changes in the Bank-rate) may be taken, as above stated, at £16,000.

In the second place, the New System would give a profit to the Bank upon the portion of its note-issues for which at present the Bank has to keep on hand an equal amount of gold, yielding no interest. Instead of having to keep so many millions of unprofitable and unavailable gold in the Issue Department, the Bank would keep an equal amount of Government securities, yielding interest at 3 per cent. The amount of gain accruing to the Bank from this change will of course depend upon the amount of its note-circulation, and cannot be stated until we see to what extent the Bank's circulation will be affected by the New System.

But, under the New System, we think it would be right that the Bank should pay interest to the State on the Government moneys deposited with it: these moneys, in truth, being the portion of its Deposits which the Bank can use with the greatest freedom, seeing that repayment of them is not called for except at well-known periods. We would still maintain the position of this great establishment as the Government Bank, but we would make it pay a moderate rate of interest on the Government moneys of which it has the use. The Bank is paid by the State for its excellent management of the National Debt; and it is only just that it should pay to the State a fair equivalent for the use which it has of the Government balances deposited with it. These amount on the average to fully 7 millions.*

* What are called the "Public Deposits" in the Bank's accounts average about 6 millions; but in this amount are not included "several accounts of magnitude," consisting of moneys held in trust by public functionaries, such as the "Chancery and Bankruptcy Accounts," — which used to be returned by the Bank as Public

The interest which the Bank would have to pay for the use of this Government money might either vary in accordance with the changes in the rate allowed by the London joint-stock banks upon money placed with them "on deposit;" or else it might be a fixed rate of low amount. Say that, on the average, the Bank were to pay interest on the Government balances at the rate of 1½ per cent:* this, on the 7 millions, would amount to £105,000 a-year,—a sum not much less than the payments which the Bank has at present to make to the State for its Charter and as profit upon the one million of its note-circulation.

Thus, financially, the Government has no motive of any consequence for objecting to the adoption of the New System. Still less, as we shall show, has the Bank of England. But, first, let us see the adverse side of the account:—

Sources of Loss.

The probable losses which the Bank would incur under the New System would arise in connection partly with its Note-circulation, and partly with its Deposits.

First, as regards the *Note-circulation.*—At present

Deposits previous to 1844, and which clearly ought to be so treated.—See Parliamentary Return, dated 7th February 1861, p. 7.

* 1½ per cent may be too high a rate of interest, even under the New System, to demand from the Bank for the use of the Government balances. But it at least puts our case in the form least favourable for the Bank; so that our statement of the advantages of the New System to the Bank cannot be said to be exaggerated. Another way of settling this matter would be to fix a certain amount of the Government balances as only adequate to compensate the Bank for its management of the public moneys, and to exact the full Bank-rate as interest on the balances above this amount.

a part of the Bank's note-circulation is absorbed by the other English banks, as a reserve to meet their daily requirements. This cannot be a large amount, even in the case of the London banks and others which do not issue notes of their own: for, as the reserve-wealth of the country is steadily increasing, *in ordinary circumstances the money paid into a bank is fully equal to the amount of money withdrawn from it.* And in the case of the English provincial banks of issue, the amount of Bank of England notes which they keep in hand must be very much less. But say that the notes of the Bank of England thus kept on hand by all the other English banks amounts, in ordinary times, to 6 millions,—probably a high estimate. Then, as under the New System, any bank may issue notes of its own, and therewith replace this reserve of Bank of England notes,—let us say that 5 millions of the Bank's note-circulation will thus be dispensed with. The result (stated in its simplest form) would be that this amount of the Bank's notes would be sent-in to the Government Clearing-House; whereupon 5 millions of the consols held by the Bank as security for those notes would be transferred to the credit of the other banks,—upon which securities these banks would, under the New System, issue notes of their own.

Secondly, as regards *Deposits.* — Nearly 10 millions (probably) of the deposits of the Bank of England belong to the other banks of the kingdom,—constituting a portion of the reserves of those banks. To overstate the case to the utmost, and thereby put the New System in the worst light as regards the profits of the

Bank of England, let us suppose that the whole of this portion of the Bank's Deposits is withdrawn. As by far the larger portion of these bank-reserves in the Bank of England are kept purely in connection with the Clearing-House, and also as a means to enable the other banks to obtain more notes when required, we may safely suppose that not more than 3 millions of these deposits will be withdrawn from the Bank in the form of gold. The remaining 7 millions would be withdrawn thus: The other banks would draw cheques upon the Bank for this amount, sending those cheques into the Government Clearing-House, — whereupon an equal amount of consols would be transferred from the Bank's credit to theirs. The consols thus acquired by the other banks would thereafter be kept by them as a portion of their reserves,—seeing that, upon these State-securities, they could issue notes to a like amount.

These changes—viz., the diminution of 5 millions in the Bank's note-circulation, and of 10 millions in its deposits—would, in the first instance (as has been shown), involve a reduction of the Bank's present stock of Government securities to the extent of 12 millions, and of 3 millions in its stock of gold.

But the greater portion of those assets would be almost immediately restored to the Bank. For, by the "running off" (*i. e.*, repayment) of the discounted bills upon which the Bank lends out the 10 millions of the reserves of other banks at present deposited with it (which reserves, we have supposed, will be withdrawn), the Bank will obtain an equal amount of money. In what form those 10 millions of the Bank's loans are

repaid does not matter. Obviously, they must be repaid either in the Bank's own notes and cheques, or in the notes and cheques of other banks, or in coin. Putting aside the amount paid in coin, as too trifling to be taken into account,* let us see what would be the effect of this operation. Probably at least 7 (out of the 10) millions of these loans of the Bank would be repaid in notes and cheques of other banks: which notes and cheques the Bank would send into the Clearing-House, — whereupon 7 millions of consols would be transferred from the credit of the other banks to the Bank of England's. The other 3 millions would be paid to the Bank in its own notes (already covered by its deposit of Government securities in the Issue Office), which notes the Bank could use as it pleased. Naturally it would invest them in the purchase of consols, which would yield interest; while at the same time, by depositing these consols in the Government Issue Office, the Bank could at pleasure issue notes to an equal amount.

In this way, of the 12 millions of Government securities withdrawn from the Bank, as the initial effect of the above-mentioned changes, 10 millions would be promptly restored to it. So that the diminution of its present amount of assets would be represented simply by a loss of 2 millions of Government securities, and a withdrawal of 3 millions of its gold.

The withdrawal of 3 millions of its gold would not occasion any loss to the Bank,—for its stock of gold yields no interest. Nor would the Bank require to

* *Vide supra*, pp. 6, 27.

replace these 3 millions of its gold,—seeing that its deposits would (*ex hypothesi*) be reduced to the extent of 10 millions, and that it would no longer be liable to any demand for gold on the part of the other banks (at present one of its most serious liabilities),—for these banks would then have taken all their reserves into their own keeping. On the other hand, the loss of 2 millions of its Government securities would diminish the revenue of the Bank by the amount of the interest on those assets,—equal to about £65,000.

Effects on the Bank's Lending-Power.

Before proceeding further, we must consider an important question which naturally arises in connection with the above-mentioned changes,—namely, What will be the Bank's power of making loans under the New System, compared with its present means? This is a most important matter: for nearly the whole profits of the Bank at present are made by means of its loans and discounts. The demand for loans would remain the same as now: it would be totally unaffected by the operation of the New System. The only question is, In what way would the Bank's power of making loans be affected by the above-mentioned changes which the New System would probably produce?

(1.) The diminution of the Bank's Note-circulation to the extent of 5 millions—in consequence of that amount of these notes being no longer needed by the other banks, which under the New System might issue notes of their own—would in no way diminish the Bank's

power of making loans and discounts. This portion of its note-circulation (as well as the still larger amount constantly in the hands of the public) is at present quite beyond the Bank's use or control,—just the same as the gold-coins which pass through the Bank from the Mint and become absorbed in the circulation of the country.

(2.) The diminution of the Bank's Deposits to the extent of 10 millions (on the supposition that the other banks would cease to keep any portion of their reserves in the Bank of England) would have a different effect. The only use of deposits to a bank is as a means of increasing its loans. If less money is deposited with it, the Bank (*quoad hoc*) can lend out less. Thus, at first sight, it seems as if the diminution of its deposits, which may be expected under the New System, would seriously impair the lending-power of the Bank, and consequently its profits. But, as we shall now show, the increased power of the Bank under the New System to issue notes would not merely compensate this diminution of its deposits, but would actually increase the present lending-power of the Bank to a very great extent.

At present the Bank's Reserve (*i.e.*, the surplus which it keeps in its banking department) in ordinary times consists of about 8 millions of notes and 11 millions of Government securities. But as these Government securities cannot be converted into notes as a means of adding to the Bank's circulation,* the *available* Reserve —the Bank's means of increasing its loans, or of meeting

* *Vide supra*, pp. 409-10.

a demand for more notes in connection with its deposits —is represented simply by those 8 millions of notes. On the other hand, under the New System, upon these 11 millions of Government securities the Bank could issue notes to an equal amount: so that the whole of its Reserve or Surplus would then be available in the form of Money. Thus, in ordinary circumstances, the Bank would have 19 millions of *money* in reserve under the New System, as against only 8 millions under the present system. It is needless to comment upon the immense advantages which would thus accrue to the Bank.

In order to show the lending-power of the Bank under the New System compared with its present power of giving banking-accommodation to the public, let us give a tabular statement,—in which we shall assume (as we have done, in order to put the case in the worst form for the Bank) that under the New System the Bank's note-circulation will be diminished to the extent of 5 millions, and its deposits to the extent of 10 millions: by which changes its ordinary stock of Government securities will be reduced from 26 to 24 millions, and its gold from 15 millions to 12.

*Under Present System.**

Liabilities.		Assets.			Surplus.	
Note-circulation.	Deposits.	Government securities.	Private securities.	Gold.	Government securities.	Gold.
22	20	26	20	15	11	8
42		61			19	

* As stated in the previous chapter, we take the Bank's note-circu-

Under New System.

Liabilities.		Assets.			Surplus.	
Note-circulation.	Deposits.	Government securities.	Private securities.	Gold.	Government securities.	Gold.
17	10	24	10	12	7	12
27		46			19	

The Bank's surplus would remain the same as at present, while its uncovered liabilities—namely, its deposits—would be greatly reduced. At present, the surplus (19 millions) is equal to 95 per cent of the Bank's uncovered liabilities ;* whereas under the New System, owing to the reduction of its deposits to 10 millions, this surplus would be equal to 190 per cent. Moreover, at present only 8 millions of its surplus exist in the form of money,—equal to 40 per cent of its uncovered liabilities ; whereas under the New System the whole of the surplus (19 millions) would be convertible into notes at will,—equal to 190 per cent, or nearly double the amount of the Bank's uncovered liabilities. Hence, as one-third is found to be an ample amount of reserve in connection with bank-deposits, $3\frac{1}{2}$ millions would be a sufficient sum for the Bank to keep in reserve so long as its deposits only amounted to 10 millions,—leaving a pure surplus of fully 15 millions *avail-*

lation, deposits, and loans at their ordinary amount previous to the Crisis of 1866. Since then, both the note-circulation and the deposits of the Bank have increased. But in so far as this increase affects the question, the result is to give a somewhat greater gain to the Bank under the New System than that stated in this chapter.

* *Vide supra*, pp. 391, 398.

able wholly for the extension of the Bank's business and profits.

It is needless to say that 15 millions of purely surplus money would not only compensate the Bank for the withdrawal of the 10 millions of the reserves of the other banks at present deposited with it, but would extend the Bank's lending-power far beyond its present amount. The only use of these deposits to the Bank, we repeat, is as a means of increasing its power of making loans: and even if a bank's deposits were all paid-in in money, and if the amount of its loans were all paid-out in money, these 15 millions of purely surplus money would far more than compensate the Bank for the withdrawal of 10 millions of its deposits. But the advantage to the Bank would be immensely greater than this: for, as every one conversant with such matters knows, it is only a mere fraction of a bank's deposits which are paid-in, or of its loans which are paid-out, in the form of money.

Consider the facts of the case. As is shown by statistics, only 5 per cent of the deposits of a bank are paid into it in the form of Money—notes or coin—(all the rest being paid-in in cheques and bills); and the withdrawals of deposits from a bank are made in like fashion.* The 10 millions of its deposits, in fact, only add about half-a-million to the Bank's stock of money—*i. e.*, notes and coin; and the same sum suffices to enable the Bank to lend out these deposits in the form of loans and discounts.† Hence the issue

* See Sir John Lubbock's banking statistics, *supra*, pp. 6, 27.

† To show how small a portion of *money* is needed by the banks in

of half-a-million of additional notes would enable the Bank to keep its loans and discounts at their present amount, despite the withdrawal of these 10 millions of its deposits. Moreover, *ex hypothesi* (*i.e.*, on the supposition that 5 millions of the Bank's note-circulation will be replaced by notes of other banks), the half-million of notes issued in these loans, not being needed in active circulation, would be returned to the Bank in the shape of deposits. So that this half-million of notes, after making these loans, would become an addition to the Bank's reserve,—which would thus again rise to 19 millions.

Sources of Gain.

The sources of gain to the Bank from the New System would arise partly in connection with its Note-circulation; partly owing to the increase of the relative magnitude of the Bank's surplus (*i. e.*, as compared with its liabilities); and also owing to a more profitable as well as more efficacious use being made of a portion of that surplus.

First, as to the Bank's *Note-circulation.*—Under the New System, every increase of the Bank's note-circulation would yield 3 per cent of profit to the Bank (£30,000 a-year on every million), instead of no profit at all, as at present. We have stated the probable diminution of the Bank's note-circulation under the New

making their loans, we may state that the entire note-circulation of Scotland (where no gold-coin is in use at all) is barely 5 millions,—a large portion of which notes, of course, are permanently in the hands of the public,—and yet the loan and discount business of the Scotch banks amounts to about 60 millions.

System at its very highest amount—namely, 5 millions. But there remains to be considered another provision of the New System which would have the opposite effect,—which would tend to *increase* the Bank's note-circulation. If (as proposed under the New System) notes for £2½ were issued, as a means of stopping the annual addition to the amount of gold-coins absorbed in the circulation of the country, these issues of small notes would amount to 5 millions each year,—equal to the annual addition to the amount of coin in circulation. Of this amount at least one-fifth would certainly consist of Bank of England notes: and this is an exceedingly low estimate. Accordingly, the Bank's note-circulation would every year increase to the extent of one million,—yielding, at 3 per cent, a steady addition to the Bank's profits of £30,000 for the first year, £60,000 for the second year, £90,000 for the third year, and so on. And if an issue of £1-notes were adopted —as by-and-by it will,—the addition to the Bank's note-circulation, and to its profits, would be very much larger. In the one case (*i.e.*, if notes for £2½ were issued), the Bank, instead of simply issuing in the form of coins a portion of the gold brought to it from abroad, would invest that amount in the purchase of consols, yielding 3 per cent, and thereupon would issue State-secured notes of its own to the required amount. In the other case (*i.e.*, if an issue of £1-notes were adopted), in exchange for the gold-coins paid into it by the public, the Bank would issue small notes of its own,—investing the gold so received in the purchase of consols (to be kept in the Government Issue Office as

security for those notes), yielding an annual revenue of 3 per cent.

Secondly, as to the Bank's *Surplus*.—It is needless to repeat that 19 millions is a uselessly large amount of reserve for the Bank to keep in connection with only 10 millions of uncovered liabilities,—namely, its deposits. What use, then, is the Bank to make of its pure surplus? Say that the Bank kept 33 per cent of Reserve in connection with its deposits,—this would be $3\frac{1}{2}$ millions; and say also that it kept $6\frac{1}{2}$ millions as a means of extending its note-issues, whether permanently or temporarily. This would leave 9 millions of the surplus at its free disposal. Now, if the Bank's circulation were to increase (for which we have thus made ample provision), the Bank would make a profit of 3 per cent on every addition to its note-issues,—instead of having, as at present, to lock up gold to an equal amount, yielding no interest. But say that the Bank's business did not increase: there would still (even after making provision for this increase) remain these 9 millions of pure surplus to be disposed of.

Let us see in what form these 9 millions would exist. Say that of the 10 millions of Reserve (kept partly in connection with its 10 millions of deposits, and partly as a means of extending its business when the opportunity offered), 5 millions were kept in gold and a like amount in Government securities,—all of which, both gold and consols, could be converted into notes at will. Then the 9 millions of the Surplus which would remain (after thus providing an ample reserve in connection with the Bank's deposits, besides

6½ millions to meet any extension of the Bank's business) would consist of 7 millions of gold and 2 of consols. The whole of this amount might be invested in the Government stock of foreign countries,—whereby it could be convertible into specie at will, while yielding to the Bank a net profit of about 4½ per cent. This would be an addition of £405,000 to the profits of the Bank,—minus £65,000 as the interest which it at present receives on the 2 millions of its Government securities: making a net gain to the Bank of £340,000. And if—as proposed in the following chapter—an International Banking-system were established (as it soon will be), this item of the Bank's profits would swell to a still larger amount.

Thus, then, without reckoning any profit to the Bank from the increase of its note-circulation (which increase, though certain to take place, cannot be accurately anticipated as to its *amount*), there would be a gain to the Bank to the extent of £340,000 in connection simply with its present surplus. The revenue of the Bank would then stand thus,—on the supposition that its circulation remains only at 17 millions, while it makes provision for 6½ millions of additional note-circulation:—

Government securities kept in Issue Office as security for note-circulation—17 millions—yielding, at 3 per cent, .	£510,000
RESERVE.	
Government securities upon which Bank can issue notes at will, by depositing them in Issue Office—6½ millions —at 3 per cent, ...	195,000
Gold—5 millions—yielding no interest, ...	0
Carry forward, . . .	£705,000

Brought forward, . .	£705,000
Foreign Government securities, convertible into specie at will—9 millions—at 4½ per cent, ...	405,000
PROFIT ON LOANS.	
Loans, &c. (as at present)—20 millions—at 4 per cent, .	800,000
	£1,910,000
Deduct interest to be paid on Government deposits—7 millions—at 1½ per cent, ...	105,000
Gross Revenue of Bank under the New System, . .	£1,805,000

From this sum have to be deducted the total costs of the establishment, including rent, taxes, salaries, pensions, cost of printing and registering the notes, &c. The cost of the present Issue Office (including the composition paid to other banks for issuing its notes) is reckoned by the Directors at the large amount of £160,000,—partly explainable by the extraordinary pains with which the Bank keeps a history (as it were) of every note which it issues. Say, then, that the total expenses of the Bank amount to £300,000 a-year:* this sum, deducted from the revenue as above stated, would leave a net profit to the Bank of £1,500,000—equal to a dividend on the 14½ millions of the proprietors' capital of fully 10⅓ per cent—which is a higher dividend than the Bank usually pays even under the present system of monopoly.†

Moreover, throughout this chapter we have stated the losses to the Bank from the New System at the highest possible amount,—alike as regards the interest

* This is a conjectural statement. The Bank, unlike other companies, publishes no statement of its working-expenses, or costs of management.

† It is an addition of nearly £200,000 to the ordinary profits of the Bank. See also *supra*, p. 403.

which we propose the Bank should pay upon the Government deposits, and also as regards the probable diminution of its note-circulation and of its private deposits. In like manner we have greatly understated the new sources of gain to the Bank,—seeing that we have put out of account the gain of £30,000 a-year (compared with the present system) on every million of additional notes which the Bank may issue: which issues, as we have shown, would probably be very large, owing to the adoption of notes of lesser value than £5.

In this way the antiquated, injurious, and untenable system of Monopoly, so far as regards the Bank of England, could be replaced by a system of freedom, not only without any detriment, but with a great addition, to the profits of the Bank-proprietors. In truth, if an issue of small notes be adopted, the gain to the Bank might be so great as to justify the State in claiming a portion of the profit derived from this source: although it must always be remembered that, under a free system of banking, every increase of banking-profits would tend to lower the rate of discount, and thereby facilitate production and increase the employment of labour.

THE SCOTCH BANKS.

The average note-circulation of the Scotch banks amounts at present to nearly five millions; and the amount of specie which they keep on hand is about $2\frac{3}{4}$ millions. Almost the whole of this stock of specie lies idle in their coffers, being held solely (under the Act of

1845) in connection with their note-issues. Their "fixed issues"—*i.e.*, the notes which they are entitled to issue without holding an equal amount of gold—amount to $2\frac{3}{4}$ millions (£2,749,271): so that, under the present system, with a note-circulation of five millions, they have at all times to keep on hand $2\frac{1}{4}$ millions of gold.

The specie which the Scotch banks actually keep on hand (as stated above) amounts to half a million more than this. But, speaking roundly, the whole of this extra half-million of specie is likewise held by them in connection with their note-issues: as a reserve, upon which they can issue more notes when these are required. They do not require to keep gold-coin for the "cashing of notes" (*i.e.*, for the purpose of giving "small change" to their customers or the public), such as is necessary in England, where there are no notes of less value than £5,—the £1-notes in Scotland serving the same purpose that gold-coin does in England. Also, the Scotch banks are but slightly connected with the foreign trade of the country, so that little demand is made upon them for gold for export. Moreover, when such a demand arises, they usually give drafts upon their agents in London in lieu of specie,—by which means the cost of transporting gold is lessened to their customers. Hence, we repeat, nearly the whole of the half-million of gold held by the Scotch banks, in addition to the $2\frac{1}{4}$ millions which they are compelled (by the Act of 1845) to keep in connection with their actual note-issues, is kept solely as a means of avoiding an infringement of the Act,—as a margin, which enables them to meet any small but sudden increase in the demand for notes.

Let us see, then, how the profits of the Scotch banks would be affected by the New System. Taking the amount of specie which they keep in connection with their present note-circulation at 2½ millions, and the rate of discount at 4 per cent, the expenses connected with their note-circulation (apart from the cost of printing, &c., which would be alike under both systems) stand as follows :—

At Present.

Loss of interest on 2½ millions of gold (kept as security for note-issues)—at 4 per cent, ... £100,000

Under the New System.

Loss of 1 per cent on 5¼ millions invested in Consols (kept as security for note-issues), yielding only 3 per cent, 52,500

Thus the Scotch banks by the New System would gain nearly £50,000 a-year on their note-issues,—or 50 per cent compared with the present burden on this part of their business. Moreover, they would also gain 3 per cent on any future increase in their note-circulation: which is an important point, seeing that the note-circulation of Scotland is steadily increasing.

THE IRISH BANKS.

The average note-circulation of the Irish banks of issue amounts to 6 or 6½ millions,—nearly coinciding with the amount of their "fixed issues," which are £6,354,494. Hence in ordinary times there is no lock-up of gold in direct connection with their note-issues. Nevertheless their average stock of gold amounts to

nearly 2½ millions. A portion of this stock of gold is doubtless necessary, in order that the banks may meet any increased demand for their notes in excess of the amount of their "fixed issues." Possibly the whole of their 2½ millions of gold may be needed in connection with their note-issues: but if this be the case, the state of matters in Ireland must be very different from that which prevails in England and Scotland; and as we have no definite information on this point, we cannot fairly assume that more than one million of their gold is actually needed by them (under the Act of 1844) in connection with their note-circulation.

On this supposition, the legislative burden or cost imposed upon the note-circulation of the Irish banks may be stated thus—taking the rate of discount at 4 per cent:—

At Present.

Loss of interest on one million of gold (kept as basis for note-issues)—at 4 per cent, ... £40,000

Under the New System.

Loss of 1 per cent on 7 millions invested in Consols (kept as security for note-issues), yielding only 3 per cent, . 70,000

The New System would thus occasion a trifling diminution of the profit of the Irish banks on their present note-circulation. On the other hand, the New System would give a clear gain of 3 per cent upon any extension of their note-circulation. And it may naturally be expected that such an increase will take place. The fact that the note-circulation of Ireland (where £1-notes

are allowed as in Scotland) is at present no greater than it was in 1844, speaks volumes as to the stagnation of that country since the great famine of 1847. In Scotland, during the same period, the note-circulation has nearly doubled. The difference in this respect between the two countries is explained by the fact that, owing to the vast emigration from Ireland, the population is at present far less than it was in 1844, while the population of Scotland, like that of England, has steadily increased. Nevertheless, despite the present deplorable effects of Fenianism, we cannot but think that the long night of Irish distress is drawing to an end, and that bright days of prosperity for Ireland are near at hand. *Then*, the exodus will cease; the unsettled state of the country, so inimical to industrial progress and so conducive to absenteeism, will be exchanged for a reign of order and contentment. And then, but not till then, will Ireland resume her growth in population, in better fashion than before: her paucity of reserve-wealth will be supplemented by the influx of capital from England; and the industry of her people will be developed, and their material wellbeing will be vastly increased. The vain regrets and criminal ambition of her agitators will then disappear amid a sunshine of prosperity which will throw into the shade even the legendary glories (so mythical) of the Past, and will evoke a spirit of contentment and loyalty before which all the efforts of agitation will gradually die away.

THE ENGLISH PROVINCIAL BANKS OF ISSUE.

The "fixed issues" of the English provincial banks of issue amount to about $6\frac{3}{4}$ millions. Beyond this amount these banks are not allowed to issue notes upon any terms,—not even upon the condition (allowed to the Scotch and Irish banks) of keeping on hand gold for each note issued beyond their average circulation in 1844. There are 190 of those English provincial banks of issue: and as each of them has carefully to keep within its fixed amount of issue, the necessary result is that their highest note-circulation falls considerably below the amount of their "fixed issues." Their actual note-circulation, in fact, is about $5\frac{1}{4}$ millions. As they are not allowed to issue more notes of their own, they have usually to keep on hand, in order to meet the requirements of the customers, a considerable amount of Bank of England notes. This amount of Bank of England notes is as unprofitable to them as if (like the Scotch and Irish banks) they had to keep an equal amount of gold as a basis for an increased issue of their own notes. But as, in the absence of official returns, it is impossible to state the amount of Bank of England notes which they have thus to keep on hand, we must exclude this element of cost from our formal exposition of the manner in which their profits would be affected by the New System.

So far as a definite statement can be made, the case of the English provincial banks of issue stands thus:—

At Present.

Legislative burden or cost in connection with their note-circulation of 5¼ millions, ... 0

Under the New System.

Loss of 1 per cent on 5¼ millions invested in Consols (kept as security for note-issues), yielding only 3 per cent, £52,500

The loss of £52,500, spread over nearly 190 banks, is a bagatelle: on the average it is barely £290 apiece. Moreover, we believe it would be much more than compensated by the fact that, under the New System, these banks would not require to keep their present reserve of Bank of England notes, which yield no interest; but, instead, would hold an equal amount of consols (upon which they would be entitled to issue notes of their own) yielding 3 per cent. Also, in their case, as in that of all the other banks, there would be a gain of 3 per cent, under the New System, upon any *increase* of their note-circulation; and a very considerable increase would certainly take place if smaller notes than those at present in use were permitted.

THE PRESENT NON-ISSUING BANKS.

Finally, we have to consider the case of the banks which at present are not permitted to issue notes upon any terms. In this category are comprised all the banks throughout the kingdom which have been established since 1844, and also all the London banks, whether established previous to that date or not. The banks

thus prohibited from issuing notes include some of the largest banking-establishments in the kingdom,—notably, the London joint-stock banks, some of which, like the Union Bank and the London and Westminster, hold deposits almost equal in amount to those of the Bank of England, and which likewise make loans and discounts to an extent little inferior to it.

At first sight, the New System would seem to confer a great gain upon those banks, yet in reality the gain would probably make but a trifling addition to their profits. Indeed it is doubtful—at least so long as no notes are permitted in England of less value than £5—whether the great London banks would avail themselves of the new power conferred upon them, seeing that cheques serve their purpose almost equally well. In so far as any of them did make use of the right of issue, it would probably be limited to the amount which they at present keep in reserve in the Bank of England as a means of supplying themselves with more notes when required. Upon that reserve at present, they get no interest; whereas under the New System, they would deposit Government securities to this amount in the Government Issue Office, and thereafter would be able to issue notes of their own to that amount, while at all times receiving 3 per cent of interest on this portion of their assets. Moreover, in addition to the ordinary reserves which they have to keep in the Bank of England under the present system, in exceptional times these non-issuing banks have to sell a portion of their reserve of Government securities, in order to provide themselves with more notes of the privileged Bank;

whereas, under the New System, they would simply require to deposit more consols in the Government Issue Office, whereupon they would be able to issue State-secured notes of their own, while still obtaining interest on those Government securities.

Such, then, would be the effect of the New System upon the profits of the five different classes of banks at present existing. On the whole, the New System would be highly favourable to the banks. Moreover, the System is so plainly reasonable, and called for by the interests of the community—as well as by the interests of the banks themselves, taken as a whole—that even though it were to occasion a trifling loss to some banks, that loss must be submitted to, in order that the currency be placed on a sound, and also on an elastic, basis.

XXIII.

AN INTERNATIONAL MONETARY SYSTEM

THE epoch of wars in Europe—that long era of strife which has lasted for more than two thousand years—is gradually coming to an end. There will be wars yet,—and possibly great wars: nevertheless the end of international strife is approaching, and Europe will ere long settle down into a peaceful community of nations,—into a commonwealth in which each State will respect the rights of its neighbours, and act harmoniously with them. The power of kings, the ambition of growing States, will ere long cease to plunge our Continent into the turmoil and dread evils of military conflicts. Each people begins to appreciate and respect the rights of its neighbours; and as the great work of national development and of self-government goes on, expediency, self-interest, will come more and more to the help of international morality. Let each people have its natural rights, and the cause of wars will be wellnigh at an end. In proportion as each nation becomes

developed and matured, as each resolves to be itself, and can manage its own affairs, this growth of the Peoples, this principle of Nationality, will raise a barrier against the efforts of selfish ambition, whether on the part of peoples or of kings. We see the beginning of this process; and though the happy end is not yet, still it is visible in the future,—it is approaching.

But there are other conflicts than those waged by armies. Industry also has its wars. The plough and the loom and the forge can engage in international conflicts of their own, without the aid of either sword or spear; and the navies of commerce can struggle in hostile rivalry, although not a cannon is fired from their decks. A war of tariffs, commercial and industrial, has long prevailed over Europe. Each country has sought to restrict or to nullify the industry of its neighbours. For the sake of its own people, it has sought to exclude the products and restrain the industrial enterprise of other countries. This warfare likewise is coming to an end. Gradually and slowly, it is true: but still the end is coming. International treaties of commerce are now the order of the day,—each country granting to the others mutual privileges, equal rights. And the natural end of this process is Free Trade in Europe: where all customs' barriers will be thrown down, and Europe will become a commercial commonwealth,—where goods of all kinds will circulate freely between country and country, and when the best goods (wherever produced) will win the day as surely as they already do in our great International Exhibitions.

But while these triumphs of peace and goodwill

among the nations are steadily going on, there is one great anachronism,—one element of our civilisation which runs counter to this happy tendency of the age. At the very time when Trade is becoming freer in communities and between nations, a form of warfare has been devised, or at least has been resuscitated in a new and more disastrous shape, which goes far to neutralise this good. While the war of tariffs is subsiding, and the conflict of States is perceptibly approaching an end, a new kind of war, alike domestic and international, has arisen within the bosom of peaceful industry,—a war which is as hostile to industry as the war of Governments is to the material wellbeing of nations. It does not affect territorial boundaries; it does not blazon its achievements in triumphal arches or imperial edicts; but it writes its dire effects in the commercial annals of every country which engages in the miserable strife. This warfare has a *Gazette* of its own. We see the record of its calamitous battles in the Board of Trade returns and in the statistics of the Court of Bankruptcy. It is a war in which no State, as a military or political power, takes part, yet in which tens of thousands of the people are forced to engage, and to suffer the hardships and losses of the conflict. There is no escape from service in that war. The most peaceful merchant at his desk, the most plodding manufacturer in his mill, is forced into the turmoil and losses of the fight whether he will or not. And for him—for all those reluctant and impressed recruits—there are no laurels. He has to fight, and comes out of the fight with his scars only: no

medals, or ribbons, or promotion. And if maimed for life, as many are, there are no pensions for him—no Greenwich or Chelsea Hospital. The power which forces him into the fray cares nothing for his losses, does not even acknowledge him in its service. He is but "food for powder" in a contest waged against his will, yet in which he is forced to take part. What is more, the myriads of our working-classes, also, are compelled to stand the brunt of this strange war. No triumphs for them: the issue is only loss,—and loss without a shadow of compensation either moral or material. They lose their wages, in whole or in part; they lose the employment which yields the daily bread to themselves and their families. It is a war, in fact, which comes home to every counting-house and almost every fireside—which affects more or less the whole industrial classes of the community: and the only results of it are losses and misery and want.

This strange new warfare—for it is a new warfare—is the War of the Banks. Ever and anon the banks of Europe engage in a disastrous international struggle. Disastrous, but not to them. They need no declaration of war by the Crown,—neither do they wait for the sanction of Parliament. They declare war for themselves, and they raise "the supplies" out of the pockets of the community. The community at large, and especially the commercial and industrial classes, are but the pawns, common soldiers unpaid for their service, with which—*i. e.*, at whose expense—the banks carry on the contest. Governments have an interest in avoiding war, because it impairs their resources; but the promoters

of this new kind of international conflict have no such motive for keeping the peace. The Banks pay themselves for making others fight; and their gains augment in proportion to the severity and duration of the conflict.

Well, then, what is this war? What is this form of international conflict into which we have of late years been so frequently plunged? Banks are, of all institutions, those which one would naturally regard as the most peaceable. How comes it that they are now so belligerent? What is the nature of the conflict into which they plunge us?—and what is its object?

Need we ask such a question? How often during the last few years have we seen this international warfare declared, this conflict waged, and the losses experienced? In 1857, as in subsequent years, in greater or lesser force, we have seen this strife carried on. In almost all cases, the Bank of England assumes the initiative in the contest: the proclamation of war has proceeded from the Bank-parlour in Threadneedle Street. The simple announcement that the Bank of England has raised its rate of discount, spread like wildfire over Europe by the wires of the telegraph, makes every bank at once stand to its arms and engage in the conflict. A weak State, when menaced by its neighbours, may yield; but the Banks do not yield. They unfailingly accept the challenge,—they at once engage in the war. Why should they not, when, whatever be the issue, the loss does not fall upon them?—and when the only certain result of the war is to augment their gains?

What is the mode of procedure?—what is the form of the war? The Bank of England raises the rate of discount: that is the first step, the declaration of war. Why does the Bank take this course? It does so, we are told, partly to prevent the export of gold, partly to bring more gold into the country. To retain or acquire a certain amount of gold—that is the motive for this international war of the banks. This European war is waged as keenly for the possession of a hundredweight or two of the yellow metal as the Greeks and Trojans closed in mortal strife over the dead body of Patroclus. "Curst be the man who first loved gold!" sang old Anacreon; and the *auri sacra fames* was deemed a bad sign of the times, a sad declension on the part of mankind, by the poet of the Metamorphoses in the Augustan era of Rome. Yet the worship of that canonised metal, discarded as an antiquated heresy in this country for a century and a half, has of late been revived in a more slavish form. And ever and anon the Bank of England adopts the most extreme measures towards the community for the sake of wringing from other countries, or of preventing their getting from us, a portion of the yellow metal so insignificant in amount as hardly to equal in value the property of not a few private individuals amongst us.

Such is the *casus belli*. Let us next see how the war, thus declared, is carried on. The Bank of England, for the sake of keeping or acquiring a certain quantity of gold, raises the rate of discount: what ensues? The banks of all other countries immediately follow suit. They also raise the rate of discount. They may have

had no pressure upon them,—and this is usually the case; there has been no special demand upon them for money, either in notes or specie; but the moment the Bank of England raises its rate of discount, they also raise theirs. In some countries the bank-rate is usually lower than it is here,—in other countries it is usually higher. But whenever the Bank of England raises its rate, the rate is raised in all other countries likewise, —(France, of late, furnishing a notable exception.)

What is the consequence? Simply this, that the position of the various banks of Europe remains unaltered. The inducement to export or import gold, between country and country, remains exactly the same as before. The result of this international war of the banks is simply *nil.* It is a game of perpetual check. A game in which every move made by one player is given "check" to by the others. And the game goes on—the Bank of England taking the initiative, and being always met by "check"—until matters come to a dead-lock; and the game ends by leaving the belligerents, as regards one another, exactly *in statu quo ante bellum.* They gain nothing from one another: the banks of one country do not attract a single ounce of gold from the other banks of Europe. The result of this belligerent policy on the part of the banks of Europe is, as we have said, as regards one another, simply *nil.* The process, so far as the international strife for gold is concerned, is absolutely useless.

This fact of itself suffices to condemn the policy nowadays pursued by the banks, and especially by the Bank of England. The policy is useless to attain the

object for the sake of which it is put in force. Instead of drawing gold from other countries, the inducement to export or import gold, as a question between country and country, remains the same as before. Surely, then, it must strike every intelligent observer that this international war of the banks is a most preposterous thing. It is commenced by the banks of some country (usually England) which experiences a casual and transient drain of specie, but as the banks of other countries instantaneously raise their rate in proportion, nothing comes of it. Even in 1864, when our minimum bank-rate was raised to 9 per cent, no gold was attracted either from the Continent or from America; and in 1866, when it was raised to 10 and 12 per cent, specie actually accumulated faster in the Bank of France than in the Bank of England.

Why, then, is this war of the banks carried on? There is no doubt there must be some motive for it, and a motive which the banks, at least, think adequate. Let us explain this motive.

The banks do attain a great end and gain for themselves by pursuing this policy. Their policy, as we have seen, is of no effect in drawing gold from one country to another. Nevertheless, there is another fact equally true: namely, that in consequence of this policy specie does ultimately accumulate in the banks—in all the banks of Europe. Although the raising of the bank-rate does not draw gold from the banks of other countries, its result is to make specie plentiful by repressing the ordinary demand for it. The war of the banks depresses Trade, and thereby lessens the demand for

Money. *Cæteris paribus*, the more trade, the more money is needed to carry it on. Check Trade, and Money at once becomes plentiful. This is precisely the principle upon which the banks nowadays act. The raising of the rate of discount by the Bank of England, being met by a similar move on the part of foreign banks, is of no effect whatever in replenishing the Bank's vaults at the expense of its foreign neighbours; but it has a most potent influence in reducing the demand for money on the part of our own community. Gold accumulates in the banks because our merchants and industrial classes can no longer employ it profitably. The only—or at least the chief, the most important, the grand—use of gold is, as international currency, to settle the trade-payments which have to be made between one country and another. Kill Trade and other forms of industrial enterprise, and the amount of those international payments is at once diminished. The war of the banks does kill Trade; this is its only effect. And not in our own country merely, but in every country where a like policy is in vogue. Hence, every season of an exorbitant bank-rate is followed by a collapse of Trade and of industrial enterprise; and specie thereupon accumulates in the banks simply because the ordinary demand for it has been checked. When the bank-rate is raised to 10 per cent, the industrial classes—whether merchants or shopkeepers or manufacturers or industrial companies—are ruined by scores. They have not only to pay an exorbitant rate for the loans and discount of bills, by which so much of our trade and industrial enterprise is carried on, but at the same

time the markets are so depressed that merchants cannot make their usual sales unless by submitting to a depreciation of their goods to the extent of 20 or 30 per cent. Hence hundreds of individuals are ruined; and the rest contract their operations to a minimum. Trade is paralysed; and money accumulates in the banks simply because it can no longer be employed. The only use of Money is to carry on Trade: and by killing trade the Banks destroy the sole object for which money exists. They make money plentiful at such times in exact proportion as they have rendered it useless. Instead of facilitating the expansion of industrial enterprise, their great principle of action nowadays is to keep it in check by repeated stranglings.

If the effect of this system pursued by the banks were to reduce the imports into any country while increasing the exports, it would at least be an intelligible policy. It would be a revival of the old "Mercantile System," which found favour in all countries in medieval times. The avowed object of that system was to promote importations of the precious metals. That was the grand object of our legislators in olden times. The wealth of a country, in their estimation, could only be increased by an increased importation and accumulation of the precious metals. The amount of specie held by a country was regarded by them as the measure of its wealth. The larger the stock of gold and silver in a country, the greater the amount of its wealth and prosperity. That was the old doctrine—the principle of the "Mercantile System;" and in order to attain this end, imports were repressed and exports were en-

couraged. Our whole commercial legislation was directed to this end. Heavy duties were imposed upon our imports, upon all foreign goods brought to this country; while our exports were promoted by means of compulsory enactments upon our colonies, and in some cases, also, by an actual bonus paid by the State upon articles exported from this country. The Mercantile System has been exploded in principle for a century; and in recent times it has been repudiated and reversed in practice by the adoption of the entirely opposite system of Free Trade. But, strange to say, while this antiquated system has been not only repudiated but reversed in our commercial legislation, it has of late been practically revived in our monetary legislation, and still more by the system pursued by the Bank of England. The repeated raising of the bank-rate to double its ordinary amount is not only justified but applauded on the very principle of the old Mercantile System,—namely, because it tends to increase the import and repress the export of the precious metals. This, truly, is a strange anomaly. While wholly banishing the principle of the Mercantile System from our commercial legislation, we have revived it, to a greater extent than ever, in our Monetary System!

But does the policy now pursued by the Banks attain the object of the Mercantile System, antiquated and condemned as that system is? It does not. It has revived the defects of the old system without attaining its object, and at the same time it inflicts upon the community injuries from which the old system was free. We repeat,—if the effect of this international war

of the banks, of the raising of the bank-rate, were to increase the exports of the country while reducing its imports, the policy would at least be intelligible. But it does nothing of the kind. It reduces exports as well as imports: it kills trade all around. As a matter of fact, it kills the export-trade first. When the bank-rate is raised suddenly (such as usually, we may say always, occurs), it has no effect in immediately checking our import-trade. But it tells immediately upon our export-trade. Merchants and manufacturers engaged in the export-trade of the country at once contract their operations. The commission-merchant (or broker) at once lessens his orders,—the manufacturer puts his men upon half-time; and the consequence is, that the amount of our exports is instantaneously diminished: and this at the very time when an increase of our exports, as a means of bringing in specie, is the very thing wanted. What more need be said? The only practical effect of the present policy of the banks is to kill trade — and to kill the export-trade first, an expansion of which would be the best and most natural means of bringing in the extra amount of specie which at such times we need, or at least are supposed to need.

Such, in its international aspect, is this War of the Banks. It is a war most profitable to those who declare it; it is a game most profitable to the banks. In proportion as they raise the rate of discount, their dividends increase. Why, then, it may be asked, do they ever halt in the process? Since, when they raise the rate from 5 to 8, 9, and even 10 per cent, their profits

steadily increase, why should they not go on, and charge rates more exorbitant still? As well ask a farmer why he does not shear his sheep twice over. A point comes, in this war of the banks, when Trade can no longer stand the pressure; a point comes when the profits of trade are swept away into the coffers of the banks, and when trade collapses under the pressure brought to bear upon it. Of late years we have been threatened, by the upholders of the present system, with a rise of the bank-rate to "15, 20, or 30 per cent;" but these are, as it were, the ravings of a madman. Experience, by repeated and lamentable facts, shows that a bank-rate of even 9 or 10 per cent is more than our trade can stand. It is killed; and thereafter the Bank has greatly to reduce its rate because it has impoverished those who deal with it. When the best and shortest-dated bills cannot be discounted under 10 per cent, it is easy to conceive what rates are charged for second-class bills, or for the best bills that have to run for four or six months. A 10 per cent bank-rate means widespread ruin and failures among our commercial and manufacturing classes, and loss of employment and actual want to tens of thousands of our working-classes.

It is strange, too, to observe that this collapse of trade occurs first, and to the most serious extent, in the very country which provokes this bootless international strife. As the bank-rate all over Europe goes up and up—the Bank of England always taking the initiative,—the event which at length stops the process is a breakdown of trade in England itself. The trade of our own country collapses first,—partly because it is subjected to the

severest trial, partly because it is far more extensive than that of any other country. Hence, we repeat, the evil which we sow we are the first to reap. The war which the Bank of England is the first to declare—which but for it, indeed, might never be waged—inflicts its losses most speedily and most heavily upon ourselves. Is this wisdom? is it civilisation? It is barbarism and folly—practised, too, chiefly at our own expense.

How we shall be pitied and laughed at by future generations! How they will mock at our vaunted civilisation! how they will deride our boastful self-gratulation! When Reform is the great cry and work of the day—when we have Parliamentary reform, Administrative reform, Law reform, Bankruptcy reform, all on our hands, engaging our minds and exercising our throats—not a word of Monetary reform! When Progress is our watchword, what will be thought of us when in one of the most vital elements of national wellbeing we not merely stand still, but actually have retrograded? When Free-trade is the cry and boast of the times—when we have indeed done a great work in that respect, and when we still more greatly boast of it,—when every trifling customs-duty struck off, or every great customs-duty slightly diminished, excites the vociferous applause of our journals of progress,—when the remission of so much duty upon foreign wines, or ribbons, or gloves, is hailed as a triumph of statesmanship,—what will future times, future generations of Englishmen, think of us when a far greater reform is never thought of, is ignored, is scouted,—and when the principle of Monopoly, the system of restriction, is permitted to flourish in one of

the most important departments of national life, and, like a upas-tree, to spread its malign influence over every branch of our Industry?

When Trade is ever expanding—when it is the grand aim of our legislation to foster that expansion more and more,—what will be thought of us when we leave the means of supporting that expansion totally undeveloped? —nay, not only undeveloped, but when we actually check it, and impose upon it restrictions unknown before? What will be said of us when one of the most vaunted of our legislative measures (the Bank Acts), not merely prevents the expansion of our monetary system so as to keep pace with the growth of trade, but imposes upon it fetters borrowed from an antiquated past, and subjects it to a regime of monopoly and restriction such as we have scouted and repudiated in every other branch of our legislation? While making Trade free by our commercial legislation, we keep it all, every branch of it, fettered and in bondage by our monetary legislation. While trade expands—when we desire above all things that it should expand—we contract the means by which alone it can be carried on. Can anything more absurd be conceived? No wonder that year by year our monetary difficulties and commercial disasters become more frequent. What else can we expect but convulsion and damage when we combine with an ever-expanding trade a contracted and inelastic currency? Our folly is like that of a man who should plant a growing oak in a vase of iron. He carefully waters and manures the tree, desiring that it should attain its amplest proportions; and he wonders why ever and anon the tree

droops or the vase is shattered. So is it with our present incongruous and incompatible systems of Trade and Banking. Trade is ever and anon strangled by the Banks; and when, as sometimes happens, our restrictive monetary system is shattered in the struggle, our legislators complacently replace the broken fetters, and leave our monetary system to strangle Trade anew!

Hitherto we have described this international conflict of the Banks—so antiquated in its principle, so disastrous in its effects—as occasioned by a drain of specie from the country (usually England) whose banks originate the war. But the war is declared and waged, also, upon another and less intelligible ground. The Bank of England frequently declares war against the banks of other countries when there is no drain of gold from this country at all, but simply an increased demand for notes. In no other country but England do banks consider such an event as a *casus belli*. The war for the possession of specie—for the sake of keeping or acquiring a certain amount of international currency—is a policy adopted *proprio motu* by banks themselves. But the cause of war of which we now speak is not primarily attributable to our banks: it is a direct and necessary result of our existing legislation. This is a noteworthy difference. The one evil is occasioned by a natural, the other by a purely artificial cause. The latter cause is simply this, that our banks are no longer permitted to utilise their credit, by the issue of notes, to meet a temporary requirement for domestic currency. Such a requirement always arises whenever there is either a monetary or a commercial

crisis. And a monetary crisis—that is to say, a difficulty (whether natural or artificial) on the part of banks to provide themselves with currency—inevitably occasions a commercial crisis likewise. At such times an increased demand for Currency takes place though the demand for Capital as a whole is actually lessened. It does not arise owing to more capital being wanted,—because, when the bank-rate is raised to a very high point (9 or 10 per cent), the operations of trade, the demand for capital, are greatly contracted. It happens (1) because commercial credit is thereby lessened, causing money to be required in payment instead of bills; and (2) because, owing to the depression of the markets, caused by the high bank-rate, merchants prefer to cash a larger portion of their stock of bills than usual, rather than lose 20 or 30 per cent by making forced sales of their goods. More of the currency issued by Banks is wanted in exchange for, and also to replace the decrease in, the currency of Trade—*i.e.*, bills. A temporary increase of bank-notes is all that is wanted. And as these notes are not meant to be cashed, and never are cashed, such a transient addition to their note-issues in no way creates a difficulty for the banks. In truth, as those additional note-issues yield a good profit to the banks, it would be profitable for the banks to issue them, irrespective of any rise in the bank-rate. But such a remedy for our ever-recurrent times of difficulty is now prohibited by the Bank Acts: and the consequence is, immense disaster to our national industry, and also an artificial cause for the Bank of England to commence that interna-

tional War of the Banks which we have already described.

Putting aside this part of the question,—this purely artificial *casus belli*,—let us deal with the War of the Banks as if it were occasioned solely by an exceptional demand for gold, and by a conflict on the part of banks for the possession of the yellow metal. And let us see if this cause of strife among the banks—as disastrous to the people in all countries as was the wrath of Achilles to the Greeks before Troy—cannot be obviated, or at least greatly diminished. Let us consider a drain of specie as a banking-difficulty under its two forms: namely, as produced either by an unusual export of gold, or by an increased demand for gold for home use. The doctrine which we preach—the economy of Capital in the form of gold which we advocate—will apply equally to both cases.

A Domestic drain of specie can be easily remedied. It ought never to constitute a serious difficulty in any well-ordered system of banking.* The specie so withdrawn from some banks is immediately deposited in others. A Foreign drain of specie constitutes a more serious difficulty: yet it also may be obviated, or at least greatly neutralised, if monetary science were rightly understood and applied by banks of issue.

The disastrous effects of a struggle for gold among the banks of Europe—we may say, of the world—we have already shown. The question now arises, how is this War of the Banks to be obviated? Can we not obviate this strife by establishing concert among the banks?

* *Vide supra*, pp. 177-180.

Can we not establish in banking, as in other things, the principles of union and co-operation, in lieu of the present system of rivalry and hostility? Even in international politics, that most unmanageable of all public questions, the principle of a Congress to settle disputes is gaining ground; and one day or other it will be established with at least some measure of success, and with proportionate benefit to the nations. In industry and finance Co-operation is already the order of the day. Mutual assistance, a combining and harmonising of rival interests and resources, is now becoming the great lever of industrial and commercial progress. It is true, co-operation among the banks of a single country, or even of a single city, is yet but little acknowledged as a principle or developed as a system. Only in rare cases, and at rare intervals, is the wisdom and practical expediency of such a principle acknowledged sufficiently to abate the antiquated system of selfishness and isolation—of every bank standing aloof in times of panic and crisis, and keeping to itself its stock of specie, whether needed by it or not.

The first fact that strikes an observant onlooker is, that at present the banks of all countries not only stand completely isolated from one another, but that they do not even make any effort to relieve the community of *their own country* from the effects of a drain of specie. They keep their reserve of securities in a form which is not available, and of which certainly they do not avail themselves, to obviate a drain of specie for export. Look, for example, at the Bank of England. The entire reserve of securities kept in its banking-department

consists of Government Stock, which, whether it sells it or borrows on it, brings it in no specie,—the Bank being paid in its own notes, which are a legal tender. The same is the case with the Bank of France—and, indeed, with the banks of all countries. Accordingly, the first means of improving the present system that suggests itself is, that these great banks should keep a portion of their reserve of securities in the form of foreign Government Stock,—in the Government Stock of those countries with which we most largely trade, and to which drains of specie usually flow,—which in our case would be Paris, Calcutta, and New York. The cashing, or borrowing upon, that stock would enable the bank to give drafts upon those places equivalent to specie, and thereby, *pro tanto*, prevent any export of the precious metals.

This would unquestionably be a great improvement upon the present system; and we hope soon to see it adopted. But such a process is clumsy and trifling compared to the improvements which will yet be made in the science of banking. Banking must assume an International form. In all departments this is the tendency of the times. The barriers of seclusion behind which communities have so long kept themselves apart from their neighbours are being thrown down. In finance—that most cosmopolitan of all trades—we already see the new system of concert freely adopted. English, French, Germans, Russians, Americans, may all be found subscribing to the same loan, or co-operating financially in the same enterprise. Banking will and must follow the same onward course. Financially,

at least, Europe is becoming one community; and one of the immediate wants of the times is the establishment of a great International Bank.

Let us look at this question, the establishment of a "Bank of Europe," in practical fashion. The financial difficulty is *nil*. The great capitalists of all countries already co-operate together freely. The only substantial difficulty in the establishment of a Bank of Europe is this,—that the great banks make a profit out of their present policy of war: their warfare with one another costs them nothing, while at the same time it is a means by which each exacts a larger portion of the profits of Trade in its own country. Well, then, let these great banks themselves establish the Bank of Europe. Let them conduct its management, frame its statutes, and divide its profits among themselves. Let the Bank of Europe be founded by the co-operation, the mutual concert, of the national banks of each country,—by the Bank of England, of France, of Holland, of Belgium, of Italy, of Turkey, of St Petersburg, Berlin, Vienna, &c.—or by such of them as are at once ready to co-operate.

Next, as to the constitution of the bank. The Banks of England and of France would probably subscribe one-half of the required capital; and each of the co-operating banks would be represented in the management, and would share in the profits, in proportion to the amount of capital which it subscribed. As regards the form in which the capital of the bank is to be subscribed and kept, this would mainly depend upon the functions of the bank. It is the natural tendency of all successful financial establishments to extend their

functions,—to widen not only the extent but the nature of their operations. But let us consider the proposed Bank of Europe in its primary form,—namely, not as a bank of deposit, or as a fountain of international paper-money, but simply as a means of conducting international exchanges of capital: as a means of economising the world's stock of the precious metals, of lessening the ceaseless and transitory ebb and flow of specie, by establishing to a limited extent a mode of international payments in Europe, apart from the export of specie. To attain this object—as we shall see more fully in the sequel—the capital of the bank need only consist of Government securities, as an adequate guarantee of its operations. Its capital would consist of Government securities of the various co-operating countries. Each of the co-operating and associated banks would subscribe its share of the capital in Government securities of its own country,—the value of those securities being reckoned by the market-price. At the outset, then—that is to say, as long as the Bank exercised only its primary functions, as an agent of international exchange,—its capital would consist of so many millions of the various Government securities of Europe (probably one-half of which would be French and British Funds), and the extent of its operations would be limited by the amount of those securities which it held.

Such a bank would be of immense service alike to the industrial, commercial, and monetary interests of Europe. Let us see how it work during a drain of gold from one country of Europe to another. As long as merchants can get bills wherewith to discharge their

debts or make their purchases abroad, they have no need of specie or of any other kind of international currency. But when, owing to a bad harvest, or the requirements of trade or finance, the amount of foreign bills in a country becomes inadequate to settle the accounts abroad, merchants and capitalists go to the banks to get specie for export. But it is a troublesome process to export specie: merchants would not have recourse to it if there were a more convenient equivalent. This they would have if a Bank of Europe were established. Instead of taking gold from the banks with which they dealt, they would ask for a draft upon the Bank of Europe,—which would serve them better, for they could transmit it as easily as a commercial bill. "Suppose, for example, that from any cause our merchants or capitalists had to transmit to Paris, St Petersburg, Constantinople, or any other place on the Continent, two millions sterling in excess of the commercial bills which we held upon those places. Our merchants or capitalists, instead of taking gold from the Bank, would get from it a draft upon the Bank of Europe; this they would transmit to the place where the payment had to be made—say Paris; thereupon the recipients of the draft would take it to the Bank of France, where the amount would either be placed to their credit as a deposit, or paid to them in the notes of the bank. The Bank of France would then send on the draft to the Bank of Europe, where the amount would be withdrawn from the credit of the Bank of England and placed to the credit of the Bank of France: and the transaction would be closed. No specie or money of any kind

would be needed. There would simply be a transference in the ledger of the Bank of Europe of two millions sterling from the credit of one of the associated banks to another's. The establishment of such an international bank, in fact, would be equivalent to *an extension of the Cheque-system and Clearing-house to the banking-system of Europe.* And the result would be a great economy of specie—just as the cheque-system and the clearing-house have immensely economised our currency of all kinds at home.

As these international bank-drafts would be preferred to the troublesome and more expensive process of exporting specie, little or no gold would be withdrawn for export from the Bank of England (or any other national bank in Europe), until the Bank had drawn to the full amount of its credit at the Bank of Europe. The amount for which it could thus draw would be the amount of capital, in the form of Government securities reckoned at their current price, which it had deposited in the Bank of Europe : and this amount could be increased at need, by the deposit of more Government stock. This would be a source of profit to the great banks ; for, instead of having to keep the present large amount of unprofitable specie to meet the wants of their customers, they would keep a portion of it (equal to the capital which they had deposited with the Bank of Europe) in the form of interest-bearing securities. When any of the associated banks (say the Bank of England or the Bank of France) had issued international drafts to the full amount of its credit at the Bank of Europe, then, but not till then, would the drain of specie upon it com-

mence. And it is hardly conceivable that any bank would subject itself to an *embarrassing* drain of specie, when it could meet the requirements of its customers more conveniently, and more profitably to itself, by temporarily adding to its deposit of interest-bearing securities in the Bank of Europe. Moreover, when a movement of specie is taking place, if there are countries which have to export specie, there are others which are receiving it in unusual abundance: so that the banks which were receiving the specie, and therefore did not require to issue drafts upon the Bank of Europe, would willingly allow their credit (or amount of securities) in the Bank of Europe to be drawn upon, at interest, by the bank from which the gold was flowing.

To those who are conversant with such matters, the effects of the establishment of such an International Bank will be fully understood by what we have already said. But for the general reader, let us say a word as to those international drafts. The great currency of the world is commercial bills. Commerce has established for itself an international form of paper-currency, which, when transmitted by post, is quite as efficacious in making foreign payments as if specie had been transmitted to a similar amount. Now, these commercial bills, although perfectly sufficient for their purpose, are not convertible into money (save optionally) except at the hands of a certain individual (the acceptor), and after the lapse of a certain period. Thus (except optionally) they are not immediately convertible into money; and moreover they circulate simply on the

credit of (at most) a couple of individuals, the drawer and acceptor. Nevertheless this currency of bills is by far the largest and the most widely-circulating of any in the world. Now, note—although it is superfluous to say so—the immense superiority of these international bank-drafts over the best possible kind of commercial bills. In the first place, they would be secured, not by the credit of individuals, nor even solely by the credit of the bank which issues them, but also by the credit of the Bank of Europe itself,—that is to say, of all the great banks of Europe,—at least to the extent of the subscribed capital of that bank. Secondly, these bank-drafts would be immediately convertible into money everywhere throughout Europe: they would be payable in cash on demand in every capital of Europe, and in every place where the national bank of the country had branches. And each holder of those drafts would receive the amount exactly in the kind of money which he required. Suppose a Frenchman or a Russian receives £100,000 in sovereigns from an English debtor, —these coins will not circulate either in France or Russia: he must take them to a bank or money-dealer, and get them exchanged for the money of that country. The international drafts, the cheques upon the Bank of Europe, will be payable in every country, and in the money of the country. In Russia they will be payable in roubles; in France, in francs and napoleons; in England, in sovereigns, or in legal-tender bank-notes to a like amount.

While economising the use of specie as international currency, these bank-drafts, it is needless to say, would

create no demand for specie on any of the associated banks to which they may be taken. Suppose a French merchant received one of those drafts issued by the Bank of England, he would take it to the Bank of France or to one of its branches, and there he would either place it to his account as a deposit, or, if he wished money, would take payment in bank-notes. Specie (except as small change) is never needed, save to make payments abroad; and the country to which such drafts upon the Bank of Europe would be sent would, of necessity, be one to which specie was flowing, and where, of course, no export of specie is conceivable. The drafts would only be issued when more money has to be sent to a particular country than there are bills upon that country; in other words, when the exchanges (indicative of the balance of trading and financial transactions) are in its favour—when specie is flowing in and accumulating, and when there is no need to send it out.

While lessening the pressure upon banks in exceptional times (now unfortunately becoming more frequent than ever), and furnishing the public with a more convenient process of making payments abroad, the new system which we propose—this development and completion of the banking-system of Europe—would impose no limitation upon the free action either of the banks or of the community. The banks would not be compelled to issue those international drafts, neither would the public be compelled to receive them. If the Bank of England, or any other of the associated banks, had a surplus stock of specie on hand, instead of giving drafts upon the Bank of Europe, it would pay out that specie.

It would only issue those drafts when its stock of specie was likely to be reduced below its normal quantity. The public, on the other hand, could always demand specie from the bank, just as at present. As such drafts would be more convenient and less expensive than taking specie for export, they would always be in favour. Nor is it easy to conceive any circumstances which would induce a man to demand specie from the bank for the purpose of export to any part of Europe if he could get an international draft instead.

Suppose, for example, that a person in this country had to pay £100,000 to a French merchant, and that the French merchant had to make a similar payment to a person in Russia; then the international draft received from England would be forwarded by the French recipient of it to Russia, and the affair would be settled: the Russian cashing the draft at the Bank of St Petersburg, or one of its agencies, and the amount being thereafter transferred at the Bank of Europe from the credit of the Bank of England to the Bank of St Petersburg's. The latter bank would then hold a larger portion of the capital of the Bank of Europe than usual, and the Bank of England would hold less. In other words, the power to draw upon the Bank of Europe and to share in its profits (*i. e.*, the interest on its Government securities, *minus* the cost of management) would be temporarily increased as regards the Bank of St Petersburg, and lessened as regards the Bank of England.

Were such a Bank of Europe established, there can be little doubt that the banks of New York and of India would also join in it: so that its operations would vir-

tually include the whole sphere of commercial and financial transactions. Ebbs and flows of specie, of course, would still take place, but they would be greatly lessened. Specie, for example, will always flow to India, and to the East generally, as long as those countries continue to export largely and to import little. It is the transient, the almost ephemeral, drains of specie which at present occasion our ever-recurring monetary difficulties. In a few months at most the difficulty is over,—the current of the precious metals resumes its old channels, obedient to the normal condition of trade and financial enterprise. But in that brief interval, what calamities befall trade under the present system,—under the policy of war and isolation at present adopted by the banks! Such drains, such transient ebbs of specie from the banks of a particular country, would be greatly lessened by the establishment of a Bank of Europe. The transient ebb would in great part be neutralised, and in natural course the equilibrium would be restored.

To what magnitude and variety of operations such an International Bank might attain in course of time we need not attempt to discuss. Of course other banks besides the great national banks (if they had an adequate motive for doing so) might likewise join in it. It would be a bankers' bank. It would be to banks what banks are to private individuals. Its deposits would be exclusively those of banks—of the leading banks of Europe. But considered merely in its simplest form, such as we have above described, the advantage of the establishment of such a bank would be very great. To

the Associated Banks it would be a boon, inasmuch as a portion of their reserve of Government securities would then exist in a form equivalent to specie,—whereas at present it is virtually useless, and is certainly never employed, as a means of providing specie. In fact a larger portion of their reserve might then be kept in the form of interest-bearing securities (deposited with the Bank of Europe, and thereby convertible into the money of all countries), and a lesser portion in the form of unprofitable bullion. To Trade, also, it would be a boon; firstly, because the international drafts would be a cheaper and more convenient means of making payments abroad than is the export of specie. But secondly, and chiefly, because it would lessen the banking embarrassment occasioned by the transient drains of gold which so frequently afflict us, and thereby would enable banks to carry on their business during those exceptional times safely and profitably, without having recourse to the exorbitant rates of discount which ever and anon cause trade and industry to collapse, which bring down good firms by the score, throw thousands of the working-classes out of employment, and check the otherwise steady progress of our national wealth and prosperity.

A reduction in the costs of banking ought always to be a proportionate gain to the community; just as a lessening of the cost of manufactures, or of the production of food, or the raw material of manufactures, is a gain to all classes. The introduction of machinery into manufactures has greatly lessened the cost of clothing and furnishing of all kinds; and a similar intro-

duction of machinery, and also of scientific appliances of manure, has likewise lessened the cost of producing food, and ere long will achieve still greater triumphs. But in order that the community may be benefited, there must be no legislative monopoly of such advantages. If only one great manufacturing firm were allowed by the State to use machinery, the community would not benefit from this reduction in the cost of manufacture. Why? Because every private firm or company naturally and invariably seeks to get the highest possible price for its goods—for the commodity in which it deals. If but one large manufacturing firm were allowed to use machinery, and all other such firms were prohibited by Act of Parliament from employing this means of cheapening production, this privileged firm would use its monopoly simply as a means of augmenting its rate of profits, and would charge as much as the other firms which were compelled to employ the more costly process of manufacture. They could not compete with it; they could not sell below their former price; neither would the privileged firm sell below it,—it would prefer to sell at the same price as the ordinary firms, and pocket all the increase of profits which its monopoly enabled it to secure. Or take another case. Suppose that three-fourths of all the arable land of the country were held by one man, and that, as under the corn-laws, a restrictive duty were maintained upon foreign corn: what would be the consequence? This man would rule the market. Having nearly all the corn of the country in his hands, he could exact an abnormally high price for it. His

selling price would not be regulated by the cost of production, but simply by the demand, the exigencies of the people: he would exact the highest price for his goods, the necessaries of life. And the few other farmers in the country, being too weak to compete with him, would willingly combine with him, and charge the same prices.

Now, what food and clothing are to the community, so is Money to all, and especially to the trading-classes. Money is as much a necessary of life to Trade as food is to the life of the community. Moreover, nowadays, in this country especially, without Trade we cannot get food. Yet, in this most important department—in our monetary system—the community can only get its wants supplied through the agency of a monopoly. A stringent monopoly is enjoyed by the existing banks of issue, which moreover are subjected to most mistaken and injurious restrictions; and until this system is abolished, the value of money will never follow the natural law of supply and demand. Hence, whatever new advantages may accrue to banks, these will be of no use to the community so long as our banking-system is subjected to a regime of monopoly. Even if, by the establishment of a Bank of Europe, the costs of banking were reduced, the public probably would not benefit one iota so long as the present monopoly of banking-currency is permitted to exist.

England is the great seat of monetary crises. As Egypt is the mother-country of the plague, and India of the cholera, so is England the prolific source of the monetary epidemics which so recurrently devastate and

oppress the trade and industry of Europe. In all questions of reform it is well to begin at home: it is well to operate first where we can do so without extraneous impediment. In this case especially, it behoves us to set our own house in order first: for it is here that the conflagration which consumes the profits of trade and industry begins. It is here, also, that the conflagration commits the sorest ravages. And the first thing to be done, is to abolish the present monopoly of banking-currency. Whatever be the conditions which Parliament may think fit to impose upon the issue of banking-currency, let all banks alike, subject to these conditions, have equal rights. Let monopoly in banking die, as monopoly in all other trades has died. Secure the currency by all means. Take whatever precautions Parliament may judge necessary to secure the validity of the note. But let all banks be equal in the eye of the law. Subject to the same conditions, let every bank alike have the power to issue bank-notes. What these conditions ought to be, in our opinion, has been already stated. But, whatever be the conditions imposed, let fair play, free trade, and a wholesome competition be established, and the great point will be attained.

Our remedy for the War of the Banks is now fully stated. In addition to the reform of our domestic monetary system, we propose to remedy the transient ebb and flow of the precious metals—those temporary oscillations which, though under the present system productive of immense disasters, no more affect the

normal equilibrium of the precious metals than the tides do the margin of the sea—by the establishment of a Bank of Europe, which would in effect be the bank for all the leading banks of the world. By means of it, the cheque-system as between banks would become international. The Bank of Europe would be the clearing-house of all the leading banks of the world. Moreover, we doubt not, in course of time, if not at once, it would become the fountain of an International Paper-money. Say that the banks connected with it, besides issuing the large drafts upon it required by merchants or capitalists who otherwise would have to export specie, were allowed to issue drafts or bills upon it down to a minimum of £10 or £20: what would ensue? The advantage to the general community would be nearly as great from this source as Trade would derive from the larger drafts. For example, any one who was going to travel on the Continent, passing from country to country, would take with him five or ten of these drafts upon the Bank of Europe, and everywhere when he presented one of these drafts (or large bank-notes) he would receive the amount in the money of the particular country in which he was then residing. He would cash one of these drafts in France, another in Italy, another in Turkey, Austria, or Russia, according to the course of his travels; and everywhere these drafts would be honoured, and paid to him in the currency which he required.

Thus the establishment of a Bank of Europe, such as we have proposed, would confer three important advantages. In the first place, and most important of all,

it would obviate, to a great extent, the transient ebbs of specie from one country to another, which at present are the bane of trade, and constitute no small embarrassment to banks. Secondly, it would furnish merchants and capitalists with a much more convenient form of making international payments than they at present possess, when commercial bills are not to be had; for instead of the troublesome process of exporting specie, they would get drafts which they could send by post. And thirdly, if drafts of comparatively small amount were issued, any tourist or traveller would obtain a supply of really international currency in a much better form than he can at present,—in fact, in the very best form it is possible to have.

An International Monetary System will certainly be established some day. The whole tendency of financial and commercial affairs is running in that direction. Our present proposal is simply an anticipation of what will be universally demanded before long.

XXIV.

SUNK CAPITAL

In our exposition of "Capital," in previous chapters, we purposely delayed considering the question of "sunk" capital: because we saw it would be more advantageous to bring it into connection, as a prelude, with the portion of our subject at which we have now arrived,—namely, State-finance, with especial reference to the effects of Taxation, Government expenditure, and the National Debt.

The term "sunk" is applied to capital in somewhat the same sense as fixed: but usually it is employed to signify wealth not merely "fixed" *quoad* its owner, but also employed in an unproductive manner—in a way which yields no return at all to its owner, and no increase of wealth to the community at large. For example, a man may sink £10,000 in boring the earth in the hope of reaching a coal-bed, or in the attempt to reach a vein of copper or tin: but if the attempt fails, if no minerals are reached, the capital so employed is sunk in every sense of the word.

The important point to be elucidated in this case is, What, financially or economically, is the effect of this "sinking" of capital? The wealth so employed is wholly lost to its owner: he gets back neither the capital sum, nor any interest on it. As regards its original owner, the wealth is annihilated: but is the capital thus parted with annihilated as regards the community at large? Certainly not. It has merely passed into the possession of others. What use its new possessors may make of it is another question: but undoubtedly they use it just the same as if it had come to them in a reproductive transaction,—*i. e.*, in a transaction profitable to the original owner of the wealth. As regards the original owner, the expenditure is a pure loss of wealth; but to the community the loss is only negative. There is no diminution of the national wealth, but there is a loss of profit, an absence of gain, in this particular expenditure, or employment of wealth. So much wealth—or, to put the case in another form, so much labour employed by that wealth—has yielded no gain, no addition of wealth, to the community. That is all. The wealth itself so expended has passed into other hands,—it still remains among the community; and the labour employed by that wealth also remains: and both the wealth and the labour may become reproductive again. In fact, the wealth in the hands of its new owners may at once employ reproductively the same labourers whom it previously employed unproductively. Hence, as regards the community at large, the only effect of an expenditure of wealth in an unproductive manner, is, not a diminution of the national

wealth, but a momentary absence of the *gain* which usually attends the employment of wealth. To the original owner, the wealth so invested is wholly lost: but it is not lost to the community,—only it has temporarily, *i.e.* on this particular transaction, made no *addition* to the national wealth. The original owner of the wealth has lost it all; the persons whom he has employed have received it in payment of their labour: hence the same amount of wealth exists in the community as before.

The sole effect of a sinking of capital, therefore, from a national point of view, is simply this, that no *addition* is thereby made to the amount of the national wealth. But no diminution of the national wealth is occasioned by it. The amount of the national wealth, at the worst, remains the same as before. The question, then, is,—What effect has this sinking of capital, this employment of wealth unproductively, upon the amount of wealth in a "floating" form—*i.e.*, in a form available for the employment of labour? It is obvious that, in this respect, unproductive expenditure has no more effect than productive expenditure,—except that in the latter case there remains the capital plus the interest or gain upon its employment, whereas in the former there remains the capital only.

Now, the negative loss, or absence of gain, which a nation experiences from any unproductive expenditure of wealth is exactly measured by the length of time during which the wealth so expended remains unproductive. This may be a matter of days, or weeks, sometimes of months. Nevertheless it is important to observe that, in countries where the banking-system is

fully developed, an unproductive expenditure on the part of individuals may, and frequently does, take place without any portion of the capital so expended being rendered for a single day unavailable for productive employment.

Let us, by some examples, show the varying effects of unproductive expenditure upon the amount of national wealth available for productive employment.

Suppose that a thousand men, on the Derby day, lose each £10 in bets to other men. The £10,000 thus lost to its owners, or unprofitably expended, simply changes hands in the form of cheques. No money is withdrawn from bank at all,—not even for a moment. The effect of the transaction upon the productive power of the country is *nil*. If the losers have to contract their business, the winners can proportionately extend theirs. At the same time, the power of the banks to give discounts or advances upon property deposited with them, remains as great as before.

But suppose, for the sake of illustrating the matter, that there is no banking-currency, whether bank-notes or cheques, and that specie or metallic currency is alone in use. Even then, how stands the case in regard to a sinking of capital,—*i. e.*, exchanges of Value (say of money for labour) which are a total loss to one of the parties? Let us say that a father gives £1000 to his son one day; that the son gives it to a brother next day; that the brother gives it to a friend on the day following; that the friend loses it in a bet on the fourth day; that the winner loses it to another betting-man on the fifth day; and that this betting-man gives it in

payment of a debt to a comrade on the sixth day. Here, then, is a series of transfers of wealth which bring no return to those who part with it: but what is the effect as regards the community? There have been six unproductive transactions, but the wealth remains. The only effect is, as regards the community, that the £1000 in specie has been lost to productive employment for a week. There has been no loss of wealth to the community: what some men have lost, others have gained. Only, there has been for a week no increase of the national wealth as regards the sum which has been changing hands. The normal state of matters is, that a profit is made on every transfer of wealth,—a profit to the individual, and consequently to the community of which he is a member. But in the case of unproductive expenditure, while there is a total loss to the original owner of the wealth so expended, there is no positive loss of wealth to the community: there is only an absence of the gain which usually accompanies transfers of wealth. And this negative loss, we repeat, is exactly measured by the length of time during which this wealth is unprofitably changing hands. The wealth itself remains undiminished, and at any moment may again become reproductive. That is all: this is the sole effect of a sinking of capital,—unless, indeed, the wealth be expended abroad, in which case, while lost to one country, it becomes an addition to the wealth of some other country.

This, we say, is the sole effect of a sinking of capital, even supposing that it were made in the form of specie. But by means of banking and banking-currency, the

series of transactions above stated could not for a single moment diminish the amount of national wealth available for productive employment. The thousand pounds, or any other sum, involved in the above series of transactions would probably not be withdrawn from bank for a single hour: and hence it would remain perfectly available for reproduction — for the employment of labour of a profitable kind. So that, while the thousand men lost £10,000, or six individuals in succession parted with £1000 without any return, the wealth of the country would not only remain as great as ever, but these sums would also remain in bank—*i.e.*, as entirely available for productive employment, for the carrying on of trade and the employment of labour, as before.

Finally, in order to reduce the question of "sunk" capital to its most fundamental elements, and to put it in the most tangible form, let us suppose that no money is employed at all,—neither cheques, nor notes, nor coin. Let us take the case of a country where the primitive system of Barter prevails, and where labour is paid for "in kind,"—that is to say, by giving to the labourers payment in goods, chiefly food and clothing. Well then, suppose, as before, that an individual employs labourers to sink a mine in the hope of reaching a bed of coal or iron: and that the enterprise wholly miscarries,—that no coal or iron is reached,—and that the result of the labour so employed is simply to make a deep hole in the earth, where no hole was needed. In such a case, what happens? The labourers so employed have been paid for their services by a certain amount of food and clothing, &c.; and that

amount of food and clothing has been used. It has been used without any return to the man who originally possessed or supplied it: *quoad* him, it is wholly lost. Nevertheless, if this amount of food and clothing had not been supplied to the labourers, these labourers could not have lived. They must either have emigrated, or else have gone to the workhouse, and been supported at the expense of the community. If they had emigrated, their labour would thenceforth have been lost to the country: the productive power of the country would to this extent have been permanently diminished. If they had taken refuge in the workhouse, the cost of their maintenance would have fallen upon the community, but their services would have been available again in better times,—though not quite to the same extent as if they had been employed by the above expenditure in sinking the profitless mine. The cost of maintaining them in the workhouse would doubtless be less than the wages they would have earned by working in the profitless mine; but, on the other hand, their effective power, when they emerged from the workhouse, would be less than if for the same period they had been employed at fair wages in the mine. Their physical as well as their moral condition would be higher, and consequently their productive power greater, if they had been so employed, than if they had been compelled to take refuge in the workhouse, and to submit to the scant fare as well as demoralising influences of that last refuge of the destitute.

Hence it appears clearly that "sunk" capital—wealth employed in labour that yields no return to its original

possessor—is by no means lost to the community. It serves to maintain in efficiency, as agents of production, a portion of the population which, but for that expenditure, must either have emigrated, or else have taken refuge in the workhouse. In the first case, this portion of the population would have been wholly lost to the country—the productive power of the country would have been diminished; in the second case, a part of the cost of maintaining those labourers would have fallen upon the community (as "sunk" capital) in the form of an addition to the Poor-rates,—and although this amount would be less than the wages paid profitlessly by the capitalist who sunk the mine, this would hardly be of advantage to the country, seeing that the effective power of the labourers would be correspondingly diminished by the scant fare and demoralising influence of the workhouse.

Such, then, are the effects of an expenditure of wealth in a profitless manner, so long as that expenditure is confined to the Home trade—to the community itself. Of course, if the wealth had been expended profitably to its owner, the expenditure would suffice not only to maintain the productive power of the country, but would also, by yielding a profit to its original holder, have *added* to the wealth of the country, and consequently to its productive power. Nevertheless, we repeat, even when capital is wholly "sunk"—*i. e.*, yields no return to its past owner—it suffices, by being transferred to other hands, to give maintenance to a portion of the population which otherwise would have to emigrate, or to become a burden on the community.

Such an expenditure, in short, though not *adding* anything to the wealth or productive power of the country, at least serves to maintain the productive power of the country at its former level. It is simply a transference of wealth from one part of the community to another.

Such, we repeat, is the effect of "sunk" capital when the profitless expenditure is made within the community itself. If the expenditure be made abroad, the result is very different. Suppose, for example, that a country *imports* £1000 worth of gunpowder, and fires it off in mere salvoes of artillery. Then the country loses this sum without any return at all: even the firing of the salvoes not giving additional remunerative employment to a single man. Even in this case, it is true, the expenditure may be useful in a political point of view (and there is hardly any form of expenditure that is absolutely useless). But, financially, it is a pure loss.

Military expenditure, the costs of war, are usually taken as the most striking exemplification of a "sinking," or waste, of capital. And if the war be carried on abroad, the expenditure, considered *per se*, is obviously more entirely lost than if the war were waged at home. For if a war be waged in a foreign country, the cost of maintaining our troops is wholly lost to our own country, and becomes a profit to the country in which the war is carried on. This, we say, is the aspect of warlike expenditure considered *per se*. Yet it is needless to add that the advantages of carrying on a war abroad, instead of at home, far more than outweigh the loss (the pure sinking of capital in military operations) which accrues from maintaining the war in another country than our

own. War is always a destroyer. It devastates the fields,—it checks or annihilates the industrial energies of the country where it is waged. It also, even when waged in the most civilised fashion, entails social hardships and sufferings, which are not the less to be deplored although they cannot be reckoned in pounds sterling.

Hence the old system of Pitt and his successors, during the great war with France, is the right one. To send an army to Belgium or Spain, and to pay subsidies to foreign Powers for co-operating with us, is the most costly form in which a military expenditure can be made. But the indirect advantages of such a mode of carrying on war far outweigh the direct loss so incurred. For thereby we not only avoid the terrible social and individual sufferings occasioned by a purely defensive war—by a war waged in our own country,—but we also avoid the destruction of property to our own people, and also the paralysis of credit and collapse of trade which necessarily must ensue, if a war is being waged on our soil. Hence, if England again has to take part in a European war, she will do well to recur to the old system, and keep the horrors and destruction of war at a distance from our own shores, by holding the foe at arm's-length,—combating him abroad, alike with our army, and by the help of friendly Powers whose aid we can procure (if not otherwise) by means of subsidies.

XXV.

STATE FINANCE

THERE are many things in the world which have a knack of being as broad as they are long: and this is peculiarly the case with State Finance. There is no science (if it can be so called) which has produced so many wind-bags—so many golden illusions, deceptive visions of an Eldorado which is never reached—grand bubbles which burst, to the bitter disappointment of the community, and to the confusion of subsequent administrators. Statesmen may dazzle the public with financial schemes which promise immense results from inadequate means: but such results never come. Or a Minister may invest a commonplace process with the appearance of a grand discovery; and he may attire it in so strange and complicated a garb that the puzzled public does for the hour regard it as a brilliant effort of

statesmanship. But strip this *rara avis* of its borrowed plumage, and it will be seen that it is but a barn-door fowl after all.

State Finance is a very plain, straightforward kind of business. Its greatest operations can all be measured and tested by the rules of plain arithmetic. No Government can get more out of a guinea than a guinea's worth. The case is different with Banking and private Finance. For these are *trades*,—operations in which money is meant to fructify, not of itself (*i.e.*, not merely by increase in the form of interest), but by the addition to it of Intellect and Labour (*i.e.*, as employed in industrial enterprise): they are transactions liable to losses as well as to gains. And with such kind of business a Government has nothing to do. A Government simply receives a certain sum from the community, and pays it away again. It is a simple receipt and a simple expenditure. And in such a case, we repeat, it is impossible to get more than a guinea's worth out of a guinea. What a Government pays with one hand, it must first receive in the other. It cannot pay off debt with the left hand without first receiving in its right hand an exactly equal value from the community. "*Ex nihilo nihil fit*," ought to be written over the doorway of every Government Exchequer.

Financial questions — many of them so complex that they may be called problems—are at the present hour rising into special prominence; and they are discussed with more carefulness, and with a greater appreciation of the facts, than at any previous period. We

do not here treat of State Finance in connection with commercial legislation—for instance, as regards the questions of Free-trade and Protection,—but of State Finance pure and simple. The burden of taxation has of late years been so vastly diminished—it is now so very much lighter than before when compared with the realised wealth of the country—that there is no urgent demand for a reduction of the existing amount of taxes: but there is a very anxious desire to ascertain whether the nation would be more benefited by a further reduction of taxation, than by keeping our Taxation at its present amount, and devoting the yearly increase in the produce of the existing taxes to the extinction of the National Debt.

Two points are raised by this question: one as regards Taxation in general, the other as regards taxation with a view to the extinction of the National Debt. We must ascertain, first, what is the effect of Taxation upon the reproductive power of the national wealth: that is to say, in what way, and to what extent, taxation hinders the national wealth from enlarging its amount by the yearly profit which all wealth may rightly be expected to yield. Secondly, we want to know in what way, and to what extent, taxation devoted to the purpose of reducing the National Debt differs from ordinary taxation in its effect upon the reproductiveness of national wealth. The two questions are indissolubly connected. Obviously no satisfactory answer to the second question can be given without a previous elucidation of the first.

GENERAL EFFECTS OF TAXATION.

What, then, is the effect of Government taxation upon the wealth, or financial condition, of a community? A right solution of this question involves the consideration of many important points,—including the use of a Government; the form in which the revenue is levied and paid; and the manner in which it is expended.

The first point to be determined is, What is the use and object of Government expenditure? A great conflict of opinion exists as to whether or not Government expenditure is to be considered "reproductive" as regards the community. Nearly all authorities maintain that it is unproductive expenditure. But in this, as in a hundred other cases of literary and political strife, the difference—at least if the disputants be aware of the true state of the matter—is merely one of terms and definitions. Government taxation is an unproductive expenditure in the same sense that wealth employed in the construction of roads may be called an unproductive expenditure,—and in no other. In the one case as in the other, the expenditure is made for a profitable purpose. True, such expenditure does not immediately and of itself make any addition to the national wealth; but it does so instrumentally,—that is to say, by enabling the main body of the wealth and labour of the community to produce greater results or profits than could otherwise be attained: which greater profits more than compensate the absorption of a portion of the national

wealth in an "unproductive" way. In both cases alike, under ordinary circumstances (*i. e.*, when the road is wanted, and when the Government fulfils the object for which Governments are established), the wealth so expended forms an advantageous investment, —seeing that it facilitates, and thereby increases, Production, or the reproductive power of the main-body of the national wealth.* It is a withdrawal of wealth from the community in order that the wealth-producing power of the community may be increased.

The Use of a Government.

What, in truth, is a Government but a means of enabling the community to exercise its energies—which is but another word for increasing its wealth—under the most favourable circumstances? A Government is like a body of watchmen delegated to ward off the danger of external attack from a working-party in a gold-mine; and also whose office it is to see that the rules of the community are obeyed, so that no one trespasses upon the ground or rights of any of his fellow-workers. If these men, these defenders and also adjudicators of the community, are neither too numerous nor too highly paid, it would be a loss to the community to diminish either their number or their pay. The cost of maintaining them is amply compensated by the service which they render.

On the other hand, if either the salaries of those

* For a statement of the great effects of Roads and Railways in economising the expenses of—in other words, promoting—Production, see *supra*, pp. 99-100.

guardians, or their actual number, be in excess of the requirements of the case, then this excess is an actual loss to the community: it is a needless withdrawal from the public of so much wealth, and from the labour-market of so many persons who thereafter are maintained at the cost of the community,—so that the producing power of the community is lessened, while its consumption remains as great as before. By reducing their Pay, the community would retain for its own use a larger portion of the produce of its industry; by reducing their Number, there would also be more labour to employ in working the gold-mine. Or, if there were not enough of remunerative work to employ these ex-officials in the mine, they would go elsewhere: in which case, the community would get no addition to its stock of Labour, but it would retain for its own use the Wealth which previously had been given to these officials.

But if, as is usually the case, the expenses of Government are no greater than is requisite for the right discharge of its functions, the wealth devoted by the community to the maintenance of its protectors and administrators is an expenditure indispensable for the due development of the national wealth. The expenses of Government, in short, are to the community a necessary means of carrying on its industry,—as much as the cost of constructing a mill is to a manufacturer, or the making of roads is to a community. It is an outlay which, far from being a loss, is a means of increasing the national wealth to a greater degree than would be possible if no such expense were incurred.

Financial Advantage of Cheap Government.

As is obvious from the preceding statement of the case, all taxation is, *per se*, a loss to the community, —inasmuch as it is a portion of wealth withdrawn from the use or enjoyment of its possessors in order to maintain a particular class, namely, the employés of the State. If the Governmental body could be wholly abolished—army and navy included—the result would be that the thousands of individuals in State-employment would thereafter be added to the producing classes, and would thenceforth support themselves; or, if they were all to emigrate, the community would thereafter possess for its use the goods or wealth which previously went to maintain the whole body of Government employés—army and navy included. The whole amount of taxation would be saved,—except (1) that portion which had been contributed by the Government employés themselves; and (2) the portion which represents the profit on the supply of goods to the State and to its employés by members of the community.

Of course no civilised community is in this Utopian condition of not needing a Government. We merely put this imaginary case in order to show clearly that (*cæteris paribus*) the smaller the expense of a Government, the better is the case for the country,—the larger is the portion of the national produce which is left in possession of the general community.

Taxation Illustrated.

The functions of a Government, and the effects of the

Taxation requisite for its maintenance, may be best shown by an illustration. Governments are fond of calling themselves "paternal" in their relations to the community: so let us suppose a family of a dozen sons, where their father acts as their guardian and adjudicator, and in return is supported by yearly contributions from them. Then the articles of food and luxury supplied to the head of the family (who does not himself engage in industrial business) constitute the expense of Government, and are so much property withdrawn from the use of those who produce it. The corn, cattle, &c., supplied to the "Governor" are consumed by him: and there is an end of the matter.

Or suppose, instead of this payment in kind, the sons give to their father bonds or paper-money, representing so much corn or so many sheep; and that by means of these bonds he obtains from his sons from time to time the commodities which he requires: in this case, also (the bonds costing nothing), the expense of Government would be exactly represented by the amount of commodities which the Governor consumes.

On the other hand, if this little community choose that, instead of paper-money, counters of gold and silver be used in those transactions, then the cost of this specie constitutes an additional expense: so that, in such a case, the cost of Government is represented by the amount of property consumed by the old gentleman *plus* the cost of the coins,—used as tribute-money by the sons, and as a means of purchase by the father. In fact, the amount of coin needed in payments to or by a State

must be included as one of the items in the cost of Taxation.

Taxation Expended Abroad.

But suppose the Governor requires to spend a portion of his revenue abroad—*i. e.*, outside the pale of his own community. Then paper-money will not do: he must either send abroad corn and cattle and suchlike commodities, or else specie. If he sends corn or cattle, he incurs the cost of freight or conveyance,—which cost necessitates an addition to the revenue which has to be paid to him: that is to say, the community must give to him more wealth than would otherwise be necessary. As specie costs less for conveyance than other kinds of property, it would, as a question of freightage, be more economical to send specie,—since the addition to the taxation requisite to pay for freightage in such a case would be less than if goods were sent. On the other hand, if specie were sent—the money being expended abroad,—the *profit* on the supply of the commodities purchased with that specie would be lost to the home-community, and would belong to the foreign country: a set-off of considerable importance.

It is true that the profit on the sale of produce, when made by a community to its own Government, is (as regards the community as a whole) quite illusory,—this profit being previously paid-for by the community in the shape of taxes. For example, let us take the case of some single million of our own revenue. If that million be spent by the Government at home, the community, in selling their goods or labour to the State, charge

thereon a certain amount of profit, as they would do to an ordinary customer: but then, this amount of profit is previously paid to the State in the shape of taxation. The State requires a certain amount of goods and labour: and if the community charge a profit on the supply of those commodities, it is obvious that the State must raise more revenue than if it were supplied at cost-price. Therefore, as regards the community as a whole, it would be as profitable for them to sell their goods to the Government at net cost,—seeing that in such a case they would have to pay proportionately less in taxation. The matter would be as broad as it is long.

But what if this million be expended by the Government abroad? The community, in that case, have to pay as much in taxation as if the million were expended at home; while the profit on supplying the State with a million's worth of goods passes to another community. For example, say that the cost-price of 20,000 sheep is £19,000, and that their selling-price is £20,000, —the profit on the sale would be £1000. The Government would have to raise £20,000 by taxation to purchase those sheep, but only £19,000 of the amount would be consumed by the State,—the £1000 representing the profit, would be simply transferred from the taxpayers at large to a particular class, the sheep-farmers. On the other hand, if this £20,000 were spent abroad, it is obvious that the £1000 would not return into the pockets of the community, but would be acquired as profit by foreigners.

Hence, financially, the question whether a Government ought to meet its own wants abroad by exporting

specie or by exporting commodities (supposing it is possible for the Government to supply its wants by the latter course), depends upon whether or not the lesser cost of exporting specie compensates for the loss of profits incurred by giving the supply of the commodities to the State into the hands of foreigners. Suppose the profit on the supply of goods to the State be 5 per cent, alike at home and in the foreign country where the goods are required: then the question whether it is more economical to export home-goods, or specie to purchase the required goods abroad, depends upon whether or not the cost of conveying specie to that country is so much less than the freightage of goods as to effect a saving of 5 per cent on the million so exported. Say that in either country 20,000 sovereigns will buy 20,000 sheep, and that the profit on the sale of those sheep to the State is 5 per cent, *i.e.*, £1000; also that the freightage of the specie is £100, and of the sheep £500. Then, if the sheep were sent abroad (say for the use of our army), our people would get the profit on supplying the sheep to the Government = £1000; but would have to pay £500 as freight. On the other hand, if specie were sent to purchase the sheep abroad, our people would lose the profit on that transaction = £1000, and also £100 as freight of the specie. In the one case they would lose £1100, and in the other £500, more than if the expenditure had been made at home. In both of those cases we have assumed that the specie or sheep are transported in a British ship: but if they are transported in a foreign ship, then there is a further loss; namely, of the *profit* included in

the charge for freight,—which, at 5 per cent, would be £5 if specie were sent, and £25 if sheep were sent.

In this way, taxation spent abroad involves a special loss to the community. In return for such expenditure, it is true, the State gets as adequate a return for its wealth as if it were spent at home. But if the Government expenditure be made abroad, the *profit* arising from that expenditure (namely, on the supply of goods or labour to the State) is obtained by foreigners: the capital so spent "fructifies" in another country instead of in our own,—the profit upon its expenditure is lost to us.

Nevertheless, it may not be *all* lost to us: a portion of it usually comes back in the course of trade. The country which receives this addition to its wealth naturally carries on more trade than before: it makes more purchases of foreign goods, and also more exchanges of commercial commodities (which exchanges are profitable to both countries),—and of this increase of international trade our country naturally gets a share, which *pro tanto* compensates us for the portion of our taxation expended abroad. How far this compensation is received depends mainly upon the extent of our trading-relations with the country where this portion of our wealth is expended. If it be made in our colonies, with which our trading-relations are comparatively more extensive than with other countries, the compensation is greater than if the expenditure be made elsewhere. For example, if it were made in China the compensation would be almost *nil:* China being so vast a region that its produce suffices for its own wants,

and its people have as yet little desire to obtain the productions of foreign countries.

But in every case, Government expenditure abroad is more or less a loss to this or to any country,—seeing that, although a perfect equivalent is obtained for such expenditure, that portion of the wealth so expended which represents the *profit* on the supply of goods to the State is lost to us. Hence it may be stated as an axiom that a given amount of taxation is more or less burdensome to a country in proportion as much or little of the national revenue is spent by the Government in other countries.

Incidence of Taxation and Expenditure.

But there are other points connected with Taxation which deserve to be noticed. One of these has regard to the incidence of taxation, the other to the incidence (if we may so call it) of the Government expenditure.

If every member of the community were taxed exactly in proportion to his means, the incidence of *taxation* would be perfect. But the wisest system of taxation ever invented fails to attain this end: so that, apart from the cost to the community as a whole arising from taxation, there is always a certain amount of financial hardship or injustice to classes or individuals, constituting an additional and inseparable evil of taxation. A still worse hardship of this kind (namely, to individuals) arises from the incidence of the Government *expenditure*. This expenditure is not equally shared-in by all classes of the community,—certainly not equally by all individuals. The consequence is, that Government expendi-

ture favours some classes or members of the community more than others.' And this, like the former, is an inseparable evil of taxation, in addition to the financial burden which all taxation lays upon a community.

We repeat, if every individual contributed to the revenue exactly in proportion to his means—or at least if he were not compelled to do otherwise (for a considerable amount of indirect taxation is simply a voluntary payment); and if, at the same time, the Government expenditure were spread equally over all classes and individuals of the community; then the cost and hardship to a community from the expenses of Government would be minimised: it would be measured exactly by the amount of taxation. But as a matter of fact, the maintenance of a Government involves also an amount of hardship (*i.e.*, special loss) to individuals, owing to the impossibility of rating every man exactly according to his means, and also owing to the impossibility of letting every man profit by the Government expenditure in exact proportion to his share in the national taxation.

Hence, of course, the greater extent to which Taxation is reduced the better, on social as well as on economical grounds. At the same time it must be kept in mind that as "Government" is simply a machinery for allowing the national energies to develop themselves under the most favourable circumstances, any reduction of taxation which tends to impair the efficiency of the Government—army and navy included—will not fail to produce to the community a greater loss than gain.

THE NATIONAL DEBT.

The interest on the National Debt is a portion of the Government expenditure which differs from the rest of that expenditure in this, that it may, and generally does, occasion no loss to the community. No portion either of the Labour or of the Wealth of the community is diminished by those payments; and hence the productive power of the country is in no way lessened. The wealth paid by a Government to its employés is consumed by these officials (so to speak) unproductively; whereas the wealth paid by a Government as interest on its Debt is as profitably employed by the Bondholders as by its previous possessors. Unlike the employés of the State, army and navy included, *the national bondholders give no labour to the Government.* The annual payment to them is for a service rendered (money given) to the State in the past: it gives the State no claim upon the services of the Bondholders; so that they are free to employ their whole labour in productive industry. Hence—supposing that, in both cases, the payments are made not abroad but to members of the same community—payments on a National Debt are less disadvantageous to a nation than are the payments for ordinary Government expenditure.

The question, then, as it first presents itself, is simply this: whether it is more economical to pay off the national bondholders by a single payment, or to continue paying to them a certain yearly sum as interest.

The special feature of the Budget of 1867 was the effort

therein made to diminish the National Debt. By the termination of the "Deadweight Annuities" the national expenditure will henceforth be lessened to the amount of nearly £600,000 (£585,740); and as the taxation of the country had during the last ten years undergone a reduction to the extent of 11 millions, it was not unreasonable to propose that the amount of the expired Annuities should be appropriated to the reduction of the capital of the Debt, instead of being made a means of striking off more taxes. The Chancellor of the Exchequer proposed to annihilate 24 millions of the Debt 18 years hence, by converting this amount into terminable annuities. In order to effect this conversion, we shall have to pay £1,776,000 a-year on this portion of the Debt for 18 years, instead of the present payment of £720,000 *in perpetuo*. The conversion, therefore, makes a temporary addition to the interest on the National Debt to the extent of £1,056,000; but at the same time, as the interest on the Debt has this year been reduced (by the expiry of the Deadweight Annuities) to the extent of £585,740, the conversion will only entail upon the public an additional payment of £470,260 for the 18 years,—by which means, in the year 1885, 24 millions of the Debt will be suddenly extinguished.

The process, therefore, is quite simple: and it entails an addition to the national expenditure which, in the present state of our finances, is trifling. We temporarily increase the payment of interest on the Debt to the extent of half-a-million, in order that thereafter we may have to pay three-quarters of a million less than we do

at present,—while the half-million temporarily added to our expenditure will likewise expire.

A Sinking-Fund.

A very keen discussion of this proposal took place in the House of Commons, but on neither side were the speeches clear or satisfactory. It was said by some of the objectors that Mr Disraeli's proposal is equivalent to the establishment of a Sinking-fund; and this charge was warmly repelled both by the Chancellor of the Exchequer and by Mr Gladstone. But if it is not a Sinking-fund, we should like to know what a Sinking-fund is. We hold that the objectors were right in regarding it as a Sinking-fund: but then we differ from them in this, that we attach no weight to the objection. We differ from them in regard to their opinion of a Sinking-fund. They regard it as an arrangement alike vicious and illusory. The old notions in regard to the potency of a Sinking-fund certainly were illusory, but there is nothing illusory in the thing itself. Disguise it as one may, we shall never pay off any considerable amount of the Debt save on the principle of a Sinking-fund. At all times, provision is made by which, whenever the current balance to the credit of Government exceeds a certain point, the amount of the excess is devoted to the reduction of the Debt, by the purchase and extinction of Consols. This, as every one knows, is an infinitesimal operation. But the moment we go beyond this point, we get involved with a Sinking-fund.

What, in truth, is the process now adopted but this,

that the country shall annually set apart half-a-million sterling for 18 years for the redemption of 24 millions at the end of that period? And is not this a Sinking-fund? The *Times*, indeed, found a distinction (and from its point of view a consolation), in the fact that "the National Debt Commissioners are but the Chancellor of the Exchequer under another name, and the scheme Mr Disraeli has adopted is but a bargain between his right hand and his left. The Annuities still to run may at any time be converted back into the Interest on their capitalised value." Well, but what advantage is there in that? Is not the same thing equally true in the case of an ordinary Sinking-fund? Cannot the Government stop the continuance of a Sinking-fund quite as much as it can make a reconversion of those Annuities? In truth such a change is more easily accomplished in the former case than in the latter. Suppose the Government became embarrassed, so that it could not afford to continue the expenditure of this half-million in the redemption of the Annuities, and that accordingly it reconverted the existing Annuities back into the form of simple Interest on the Debt. It is certain that at such a time the money-market would be in a bad state: so that the probability is that the reconversion could only be made at a loss. On the other hand, suppose Parliament had simply passed a resolution to the effect that half-a-million be set apart annually for the redemption of the Debt: this resolution could in an emergency be suspended at any moment, and no loss could possibly occur.

In this respect, the plan proposed by the Chancellor

of the Exchequer, and adopted by Parliament, is actually less convenient than a pure Sinking-fund. If Parliament had established a Sinking-fund by pledging itself to vote half-a-million every year for the extinction of the Debt, in an emergency Parliament could simply decline to make that annual vote,—and there would be an end of the matter. But if, as now arranged, 24 millions of Debt are converted into terminable annuities, in an emergency the only way of getting out of this annual payment of half-a-million is by reconverting the annuities into Consols,—*i.e.*, into the old form of simple interest on the Debt,—a process which is almost certain to be accompanied by a trifling loss. True, such an emergency may not arise: it is not probable that this country will be so greatly embarrassed that the payment of this half-million will have to be cancelled as too heavy a burden: nevertheless, we repeat, if such an emergency were to arise, the present system would be less advantageous than an ordinary Sinking-fund.

On the other hand, a Sinking-fund in the form now adopted has two great points in its favour,—not financially, indeed, but as a matter of political convenience. In the first place, it removes this half-million out of the category of debatable expenditure. This sum will not be counted as part of the annual surplus: the Government will not be worried with applications for devoting it to the reduction of particular taxes. In the second place, by operating upon 24 millions at once, a great eventual boon is kept before the eyes of the public, as a worthy object of the small temporary self-denial

required of them. If half-a-million were taken annually from the surplus, and devoted to the redemption of an equal amount of Consols, the result could be made financially as great as will be attained by the scheme now adopted. But the extinction of a mere half-million of the Debt would be a very small matter in the eyes of the public; and the House would be ceaselessly tempted to devote this portion of the surplus to other purposes,—especially to the very tangible advantage of reducing some particular tax.

Financially there is no real difference between the present proposal and a Sinking-fund. Men may confuse and delude themselves by verbal jugglery, until the same thing becomes in their eyes something very different; but there is no real change. A Minister may dress up a Sinking-fund in another attire and call it by some other name, nevertheless it is a Sinking-fund still. But we repeat, if Debt is to be paid off, there can be no valid objection to a Sinking-fund. It is the only means by which a permanent machinery for paying off Debt can be established. True, at one time the most exaggerated ideas of the efficacy of a Sinking-fund were current. It was looked upon as if it were a magical machine, by putting a sovereign into one end of which the coin came out at the other end multiplied twenty-fold. And no doubt, if a Government does not use its money for so many years, it will at the end of that time have in one sum both the capital and the accumulated interest. But if the Government had used the same money from year to year in the purchase of Consols, retaining for itself the interest on those

Consols, it would have reaped quite as much value as it can do by spending the capital and accumulated interest all in a lump at the end of the period. In fact, whether half-a-million be annually included in the Budget, as a yearly vote for reducing the Debt, or whether a like sum be raised to meet a fixed charge on the country for the same purpose, comes economically to the same thing. By no financial jugglery, we repeat, can a Government get more than a guinea's worth out of a guinea. When the old Sinking-fund was in its heyday, people fancied that this could be done; but as soon as this notion was dispelled, a revulsion of sentiment took place, and thereafter every Minister or financial authority has thought it a clever and correct thing to denounce a Sinking-fund as an error and an illusion. It is nothing of the kind. Like everything else, it is good for what it is worth: it cannot work marvels, but it can be of use.

Creation of a National Debt.

A National Debt creates a permanent addition to the Taxation of a country. There can be no question that a nation (like a company or a private individual) is justified in meeting an exceptional expenditure, designed to benefit the future as well as the present, by partially anticipating the profits of future years. A war is to a nation what a great fire is to an insurance company, or what a great destruction of works by an inundation is to a railway company. It is an exceptional disaster, the cost of which may rightly be spread over several years. The cost must be met immediately

—or else the country, like a company, must undergo far greater losses: but the payment of a large portion of this outlay may legitimately be thrown upon the revenue of future years.

This principle cannot be questioned. The only practical question is, How much of the exceptional expenditure should be met by a contemporaneous addition to the Taxation, and how much may properly be raised by loans, the interest of which will constitute an addition to the Taxation of future years? This is not a question which can be decided by any absolute or theoretic rule. It is a question which must be determined according to the special circumstances of the time. It is a question of Statesmanship, rather than of Finance. As such it is beyond our province. Nor indeed can any Minister, even though gifted with the highest powers of statesmanship, decide such a question in advance, and simply on theoretic grounds.

Is it an Economy to pay off the Debt?

Although it is beyond the province of pure Finance to dogmatise as to the circumstances under which it is right for a State to contract Debt, a most definite and important financial problem arises in connection with the question, How far, and under what circumstances, is it advantageous for a country to pay off its Debt?

A curious and important point connected with this question was raised by Mr Gladstone in his speech in support of Mr Disraeli's plan (which was also his own) for paying-off a portion of the National Debt. Mr Laing had remarked briefly, and without going into

any arguments in support of his opinion, that "a nation, like a great landed proprietor, might adopt either of two principles in dealing with its liabilities. It might either better its position by paying off the debt in instalments; or, continuing the payment of the interest on the debt, it might apply all the surplus revenues to the improvement of the estate." This remark appeared to Mr Gladstone a serious heresy, and drew from him the following reply:—

"The hon. member tells us there are two systems, which he places in contrast one with another, and with regard to which he leaves his own preference not a subject of much doubt. One of these systems is, diminishing your debt; the other is, leaving the money with which you would otherwise diminish debt to fructify for the benefit of a nation through the reduction of taxes. Now, it appears to me that that is not a just or a true statement of the case, and that when you talk of the "fructification" of money—I accept the term, which is originally due to very high authority—there is none much more direct and more complete than that which the public derives from money applied to the reduction of the debt. For what becomes of that money? It is not sent to the moon. It is not exported from the country. It finds its way into the money-market of London, where loanable capital obtains the most direct and profitable employment in cheapening production and stimulating industry. In my opinion, therefore, it is an entire fallacy to suppose that the question lies between the diminution of debt and allowing your capital to fructify. I contend, on the contrary, that there is no surer method of promoting an immediate and profitable application of capital than by reducing debt."

Financial problems, although they may be simple when one gets at the heart of the question, are exceedingly puzzling at the first blush. A great deal of careful consideration is necessary before we arrive at the

results; and even after one has attained to a definite view of the case, it is exceedingly difficult (owing to the complex nature of the subject) to state the results in clear and simple language, adequate to bring home the facts clearly to the mind of the public. Hence it was only natural in the circumstances, that a speaker dealing with the matter off-hand should get mystified as he involved himself in the question: and Mr Gladstone certainly did so in his further remarks. He ended by confessing that he had not proved his case, and was not competent to elucidate "so complicated a matter" on the spur of the moment. But the gist of his opinion is stated clearly enough in the extract which we have given. And from that opinion we differ. There is a grain of truth in it, as we shall show: but on the whole question the opinion of Mr Gladstone is disproved by the facts of the case.

Mr Gladstone is clearly wrong in his general proposition,—namely, that the paying-off of debts is the most profitable way of employing money. Our whole trading-system, in fact, is based upon exactly the opposite principle. Our vast trade is carried on by means of contracting debt,—by getting credit. A merchant, speaking generally, is only too glad to get credit (*i. e.*, to incur debt) as a means of extending his business. Say that he gets a loan at 5 per cent, and employs the amount in extending his business: he obtains on the sum so employed a profit (made by the employment of his skill and labour) of 10, 15, or 20 per cent,—so that, while paying interest on the loan, he reaps in addition a profit of 5, 10, or 15 per cent on the sum

which he has borrowed. Clearly, then, as regards the transactions of private life—as regards the general community who employ their money in business of one kind or other—the paying-off of debt is *not* the most profitable means of using wealth. On the contrary, by such a process our Trade would at once be immensely contracted, with great loss to the wealth-producing power of the community.

At the same time, it must be remarked that Mr Laing's parallel between the case of a landed proprietor and that of the State is glaringly imperfect. A landed proprietor, or other private individual, *trades* with the money which he has obtained on loan. A State, on the other hand, does not, and ought not, to engage in trade. Accordingly, money does not "*fructify*" in its hands. And Mr Gladstone, in the above extract, acknowledges this: he takes it for granted. He puts his case upon another footing. He maintains that the money spent by the State in extinction of its debt, becomes thereafter more available for productive employment by the public—it "fructifies" more readily and potently—than money spent by a trader in extending his business. He says:—"It finds its way into the money-market of London, where loanable capital obtains the most direct and profitable employment in cheapening [by facilitating] production, and stimulating industry." Undoubtedly it does so in the main: but the question in point is, To what extent does money spent by the State in extinction of debt do this more than money expended in the improvement of property or in the extension of trade? Let us examine the facts.

If a million of debt is to be paid off, the State must raise by taxation a million more than is required for the ordinary expenses of Government. The State pays this sum to a certain number of persons who hold State bonds (which bonds are thereby cancelled), and thereafter the million sterling is employed by its receivers (the ex-bondholders) in trade or other kinds of expenditure. Now, the sum would have been employed in the same way by its original possessors (*i. e.*, the public), if it had not been withdrawn from them in the form of taxes. Thus far, then, there is no difference: except in this, that, when paid to the State, this employment of the money *may* take place less quickly than if the sum had remained in the pockets of the public. At first sight, in truth, there appears to be a loss on the transaction, represented by the length of the interval during which the sum is being transferred by the State from its old owners to its new ones,—from the taxpayers to the bondholders. But, thanks to the banking-system, no such loss occurs.* The sum, though temporarily unemployed by its owners, lies in bank, available for the use of others.

Thus far, we repeat, there is neither loss nor gain on the transaction. But another point has to be taken into account. The million raised for the extinction of State Debt is collected by taxation in driblets from many thousands of individuals, but when paid in extinction of the Debt it passes into the hands of only a few persons. At first sight, this appears to be an advantageous result as regards the "fructification" of wealth:

* *Vide supra*, pp. 108-12, and 138-40.

for, speaking generally, wealth becomes more available for the employment of labour when concentrated in a few hands than when diffused among many possessors. But there are two points which, in this case, invalidate such a conclusion. Owing to the banking-system, the spare wealth of the country (*i.e.*, the amount of wealth not needed by its owners for their own consumption) is all deposited in bank, and therefore is available for the employment of industry just as fully whether it belongs to a thousand owners or to one. And if it be said, in opposition to this, that though the statement be true in the abstract, nevertheless, when a given sum is diffused among a number of small owners, the portion of it *not* in the bank, but which each man keeps in hand for his daily wants, is larger than if the sum were in the possession of a few large capitalists: it must be borne in mind that each member of the wealthy classes keeps in hand a far larger amount of money than a member of the lower-middle or of the working-classes does. A holder of Consols keeps ten or twenty pounds in his purse or at home, while the labourer does not keep as many shillings. Hence, the fact that a portion of the million of revenue used in extinction of State Debt is raised from the poorer classes, and is transferred into the hands of persons comparatively wealthy, is not of any appreciable importance in determining the relative economy of paying-off Debt, or of leaving an equal sum undisturbed in the hands of the community.

It thus appears (1) that the money invested in the extinction of Debt is employed by its new owners in another way than it would have been if it had remained

in the pockets of the public; (2) that the interval during which this wealth is being transferred from the public to the State-creditors would occasion an actual loss on the operation, were it not for our banking-system; (3) that though the sum is collected (by taxation) from thousands of owners, some of them comparatively poor, and is paid into a few hands, comparatively wealthy, this does not affect the reproductive power of the sum in question,—seeing that in this country all spare wealth, whether held by high or low, is deposited in bank, and therefore is equally available for the employment of industry.

Manifestly, then, Mr Gladstone's proposition that the paying-off of Debt is a more economical process than allowing the money to "fructify" in the hands of the community, is a fallacy, even in its most tenable form —namely, when the amount paid in extinction of the Debt is not paid to foreign creditors, but simply transferred from some members of the same community to others.

Question affected by the Rate of Interest.

But another fact (antagonistic to Mr Gladstone's proposition) remains to be noted. The peculiarity of the National Debt of this country is, that the rate of interest payable on it is lower than the ordinary rate which prevails either in this or in any other country. This fact of itself constitutes an important element in the question whether our surplus—*i.e.*, the yearly increase in the produce of the existing taxes—should be applied in extinction of the National Debt.

Our National Debt, like that of other countries, represents an amount of wealth which belongs partly to our own people and partly to foreigners. By far the larger portion of the Debt, almost the whole of it, belongs to our own people; nevertheless, as a part of it belongs to foreigners, this latter portion must be taken into account, and dealt with separately: for the question of paying it off involves other considerations than those which relate to the portion of the Debt held by members of our own community.

First, then, as to paying-off National Debt which has been lent to our Government by, or which now belongs to, foreigners. By paying-off such debt, the nation loses a portion of the wealth which it can use in trade or in other forms of productive investment; but, in return, the nation is released from payment of the interest on that amount due to foreigners. Hence, the financial advantage of paying-off such debt depends entirely upon the rate of interest which is payable on the Debt. If that rate of interest were higher than the ordinary rate in this country—*i.e.*, if it were such as partially to absorb the ordinary profit on the employment of wealth—then, unquestionably, the sooner the capital sum is paid off the better. On the other hand, if the rate of interest payable on such debt is less than the current rate of interest in this country, then the paying-off of such debt would financially (and at present we are considering the question simply from a financial point of view) be a loss to this country. We should part with a portion of the wealth at present in our keeping, and which we can employ at a profit. Although we have to pay interest

on it to its foreign holders, so long as this wealth can be employed at a higher rate of interest by ourselves, it is simply a loss to return it to its owners. This, then, is the financial aspect of the question, as regards paying-off National Debt which has been advanced to us by individuals in other countries. It would be simply to send out of the country so much capital which we can employ at a profit.

Secondly, as regards the portion of the Debt which is held by our own people. This is the most important part of the question, since nearly the whole of our National Debt is held by members of our own community. In this case, to pay off debt is simply to transfer the amount from the general public, from the body of taxpayers, to the particular class who are the bondholders. The wealth withdrawn from the general public for this purpose is a subtraction from their power of production—from the wealth which they can employ in trade and industry of all kinds; but at the same time it is an equal addition to the productive power of the bondholders, who can employ it in trade just as well as the general public can. Hence the paying-off of such debt neither increases nor diminishes the productive power of the community. It is simply a transference of wealth, which can be employed as profitably by its new possessors as by its old ones.

In this second case, it matters little what the rate of interest on the debt may be. For at most, it involves a transference of profit from one part of the same community to another. If the rate of interest on the Debt be ever so high, what some classes lose another class

gains. So that, in a national point of view, the result is *nil.* At the same time, the object of sound legislation is to insure to all classes alike an equal profit on their wealth or labour: and if the annual charge on the Debt be higher than the ordinary rate of interest, then the State should seek either to diminish the rate of charge, or to diminish the amount of the Debt. For example, if during a great national emergency (such as the late Civil War in the United States), a Government has been obliged to borrow at an exceptionally high rate of interest, it is the duty of that Government, as soon as ordinary times return, to reduce that annual charge as fast as possible,—either by conversion of the whole debt from a higher to a lower rate of interest, or (if that be not practicable) by paying-off as much of the debt as possible. For, even though the debt is held by members of the same community, so that there is no national loss in the transaction, the general public is forced to pay to a particular class a larger amount of interest than is payable on contemporary loans, or which would be equitable if the debt were to be contracted anew.

In the case of our National Debt, however, the annual charge is so low that the bondholders derive no gain at the expense of the community at large. If 50 millions were called up from the general public, in taxation, in order to pay off an equal amount of our National Debt, the taxpayers would certainly lose by the transaction as much as they gained.

The Question of the Future.

But this does not exhaust the financial question: there still remains the element of the future. Although it is true that it would be no financial gain to the public to pay off any portion of the Debt, simply with a view to the present, it does not follow that it would not be a gain to do so as regards the future: for, if no reduction of the Debt be made, it is possible that emergencies may arise which will necessitate the contraction of fresh debt upon terms disadvantageous to the general body of the community.

The larger the debt of any country, the less, *cæteris paribus*, is the State's credit or borrowing-power. In other words, the greater is the State's difficulty of obtaining loans, and consequently the higher is the rate of interest which it has to pay on them.* Now, the credit or borrowing-power of a State is a most important element of the national strength. In times of war, loans are indispensable. These are exceptional times of emergency when a community must draw upon the future, —must appropriate in advance a portion of its future gains. Just as a trader tides over a temporary difficulty by pledging a portion of his future annual profits, so it is convenient for a State to do likewise during an exceptional emergency, such as war. Hence it is wise for a State in periods of peace to reduce the amount of its Debt, in order that, when further loans become necessary, it may be able to obtain them at no higher charge than before.

* *See infra*, pp. 556, 557.

Political Considerations.

Even as a simple financial question, therefore, it is advisable for States to pay off Debt, in order that they may not have to pay an increased charge upon further loans, which may become necessary in the future. But *politically,* this consideration is far more important: for in times of national emergency, the promptitude with which a State-loan can be raised constitutes as great an element of national power as the promptitude with which a State can augment its army or navy. In fact, in many cases, the two operations must go hand in hand.

Moreover there is another point of this kind to be noticed,—namely, the moral influence of a reduction of the National Debt. In matters of Finance, moral influence plays a most important part,—as any one practically conversant with such affairs knows well. The same securities or other kinds of property sell at one time for only half the price which they bring at another, without any alteration in their intrinsic value, but simply because a spirit of hopefulness and confidence prevails at one season and a spirit of despondency and distrust at another. A country which sets itself to reduce its National Debt always has this moral influence strongly on its side. The general tendency of a National Debt is to increase; and in truth it may increase without (thanks to the increase of wealth and population in the country) in any way becoming a proportionately greater burden. But when a country, especially one so progressive as ours, sets itself to reduce the amount of

its Debt, the moral effect produced is very great. And this moral effect is no mere abstract advantage, for the gain may be definitely measured in the solid form of pounds, shillings, and pence. The more fully a State possesses the confidence of the public, the more easily is it able to borrow: and no State can borrow on such easy terms as one which proves its financial prosperity by reducing its Debt, especially in circumstances from which it has so little to gain as ours.

The Question as it affects Fiscal Reforms.

There is yet one more point to be noticed. In most cases it is better to make a large reduction of the Debt in a given year than to effect a similar amount of reduction by petty annual payments spread over a number of years. As a fiscal question, it is better for the public that the extinction of Debt should be made in the form of Annuities which will expire in a given year, than by devoting to the same purpose a small sum annually. For, in the latter course, the gain is too small to allow of any important change being made in the taxation of the country; whereas, when a large reduction of expenditure can be made at once, as by the expiry of the annual charge on these annuities, the Finance Minister of the day has so large a surplus in hand that there is hardly any change in our system of taxation too extensive for him to grapple with. For example, there can be no doubt that the Malt-tax is opposed to principles of economical science now fully established: but then, the tax produces so much—it forms so large a portion of the Revenue—that the very magnitude of this fiscal

injustice serves to perpetuate it. It is one of the advantages of the method of reducing the National Debt now adopted, that, ere long, by suddenly leaving a great surplus in the hands of the Finance Minister, it will enable him to effect reforms in our taxation of the most important kind, and which but for this method of procedure would be too extensive to be undertaken.

XXVI.

THE STATE AND THE RAILWAYS

THE serious embarrassments which have recently befallen Railway Companies have brought into prominent importance several great questions in regard to Railway Finance. Some of those questions relate to railway management and accounts; others are of a wider and more important character,—their object being to determine the relations which ought to be established between the State and the Railways. In past years the question was ever and anon raised as to whether the State ought not to buy up the Railways as a means of increasing its revenues,—as a measure highly profitable to the State: and the chief difficulty which presented itself was the probable reluctance of the Railways to submit to any such interference. But now the question has somewhat changed its complexion, and the interference of the State has been demanded chiefly in the interests of the Railway Companies themselves,—as a means, in fact, of releasing some of them from their present embarrassments.

We shall commence our remarks on Railway Finance by considering the relations which ought to be, or might be advantageously, established between the Railways of this country and the Government.

Regret has frequently been expressed of late years that, at the outset of railway enterprise, our Government did not take into its own hands the construction of railways,—or at least that it did not stipulate, in return for facilitating the construction of railways, that these works should, after the lapse of a certain period, become the property of the State. The question of proceeding in this manner was considered by Sir Robert Peel in 1844; but he decided not to adopt it. Let us consider this decision. Obviously there are many objections to a Government like ours, or indeed any Government, becoming the sole agent for the management of so vast a railway-system: objections founded alike upon the inexpediency of placing so vast an amount of patronage in the hands of the Executive, and also upon the fact that it is exceedingly doubtful if the State would manage the railways as successfully as the present Boards of Directors, who have a personal interest in working the lines economically and efficiently. Passing over these objections for the present, let us consider the question simply on financial grounds.

In the first place, upon what grounds could our Government have exacted such terms from the railway companies? Upon what grounds could the Government have claimed that the railways about to be constructed should, after the lapse of 99 years, or any other

period, become the property of the State? In France, the Government paid large "subventions" to the railway companies; but no Government aid of any kind was given to the railways of this country, which have been constructed entirely by private enterprise. Or take the case of India. There, the land belongs to the Government,—so that, in lending it to a railway company, the State might justly exact some return: in truth the accumulated rent of the land, principal and interest, would at the end of 99 years amount to an enormous sum. Nevertheless the Indian Government makes no claim for the ultimate possession of the railways: and in England such a claim would have been simply preposterous. In England the State has no property of its own to give; and the companies have to purchase the land which they require from private individuals. In short, in this country the State can make no claim at all, whether immediate or prospective, upon the property of the railways,—seeing that it gave nothing to the companies, whether in money or in land.

Mr Laing maintains (without giving any grounds for his opinion) that the State ought either to have stipulated that the lines should, after a certain period, become the property of the State: or else that we "ought to have gone on the American plan of total free-trade in railways:"—which means, we presume, that any company ought to have been allowed to construct a railway in any locality without requiring to obtain the consent of Parliament. To both of those opinions we demur. The adoption of the first of Mr Laing's alter-

native proposals would (as above shown) have been an act of gross injustice on the part of the State; the effect of which would have been most seriously to impede the construction of railways in this country. Nor would the second course have been of any use to the companies, especially at the outset of railway enterprise.

For in truth, what does this consent of Parliament amount to? The main object of a Railway Act is to obtain compulsory powers to purchase the land necessary for the construction of the railway. In a thinly-peopled country like America, where railways often traverse unoccupied districts, and where they are as much the pioneers of civilisation as its followers, there has hitherto been no difficulty in obtaining land for a railway,—a large portion of the land, in fact, being unoccupied ground belonging to the State. But in this country the case is quite different. Every inch of the soil is fully occupied; and every foot of it belongs to private individuals, all of them jealous above measure of any infraction of their rights. Hence, if the "free-system" had been adopted in this country, it is a matter of fact and of history, rather than a mere opinion, that, at the outset, hardly any railways could have been constructed at all. Railway Acts, in truth, instead of being hindrances, as Mr Laing seems to regard them, were indispensable to enable the companies to obtain by purchase the lands which they required. These Acts were, every one of them, interferences with the right of private property: that was and is their prime object. And the power which Parliament reserves to itself of saying whether or not any particular line shall be con-

structed amounts simply to this: that Parliament declines to use its dictatorial power of compelling owners of land to sell their property unless there is a good case made out in the interests of the public for Parliament to employ this exceptional power.

Nevertheless it may be argued that since the State, in the interests of the public, gives a compulsory power of purchase to railway companies, to enable them to get possession of the land which they require, the State, on the same ground of public interest, may require from those companies an ultimate cession of the land so acquired, and also of the permanent works which may be erected upon it. Obviously, this is a very heavy price to exact for the mere power conferred upon the companies to purchase the land which they require at its full value. Mr Crawford, it is true, maintains that the burden so imposed upon railway companies would be little felt by them. He says that if a railway company were to establish a sinking-fund by which 20d. for every £100 of their capital (or something less than £1 in every £1000) would be set apart every half-year, and invested at 3 per cent, the produce of this sinking-fund would at the end of 99 years be sufficient to replace the entire capital of the company: so that, while then handing over their railway to the State, the shareholders, by dividing among them the produce of the sinking-fund, would simultaneously acquire the full value of their property in another form. Thus, by being spread over so many years—three generations—the burden would be little felt. This sounds plausible enough: but it cannot alter the hard financial facts. A 99 years' lease of a

property certainly will not sell for as much as the freehold of that property. Indeed it is obvious that any gain which is worth the State's getting, is worth a Company's keeping. Hence, apart from the fact that all such long-dated arrangements are cumbrous and uninviting, there can be no question that, with such a prospective burden upon their profits, railway companies would not have been so readily established. In consequence, the development of railway-communication in this country would have been sensibly retarded.

Now, this would have been a negative loss to the country of a very serious kind. As railways are a most potent means of facilitating and cheapening production of all kinds, the slower progress of our railway-system would have been accompanied by a slower development of our trade and productive industry: and this would have been a loss to the community, and likewise to the State, which we believe would have much more than counterbalanced the gain to the State in obtaining possession of the railways at the end of 99 years. And so Sir Robert Peel obviously thought. To facilitate production, and with it the employment of the people, was the main object of the Peel policy: and to retard the construction of railways by imposing hard terms on the companies would have been a fatal mistake. The small annual loss or lock-up of profits, on the part of the companies, would indeed return to the companies in the third generation; but that would have been no consolation to the original shareholders, the persons by whose capital the lines were to be constructed. For my own part, I regard it as certain that

the slower progress of our railway-system under such an arrangement would have retarded the progress of trade and production to an extent that would have more than counterbalanced the proposed gain to the State at the end of 99 years. And this, altogether apart from the question whether, when the railways did at last come into the hands of the State, they would be as well managed as if they were to continue in the hands of private companies directly interested in their economical management.

It is of little use, however, to discuss what might have been done in 1844. The point is, what is it advisable to do now? Unquestionably, if any change is to be made, now is the time for it. If the State desires to intervene in Railway matters, it can do so at present upon better terms for itself, and with less opposition from the railway companies, than are likely to recur.

The pressing want of the railway companies at present arises from the difficulty which they experience in meeting the payment of their debentures; and this difficulty necessarily occasions a depression in the value of Railway property as a whole: that is to say, railway-shares no longer bring their usual price in the market. This, of course, gives an opportunity to the State to acquire possession of the railways on exceptionally favourable terms. Hence it has been proposed that the Government, while intervening to relieve the companies of the difficulty in connection with their debenture debts, should do so in such a way as to obtain ultimate possession of the railways themselves. This is the

twofold object which Mr Crawford has in view, in his proposals. Let us examine each branch of this object in succession. We shall state the matter as briefly and clearly as is possible.

Mr Crawford's Plan.

I. Mr Crawford proposes that the Government should take upon itself the whole debts of the railway companies, or of such of them as desire this assistance. The State is to withdraw the existing railway-debentures, and issue to the holders of them Government bonds for an equal amount, bearing interest for 50 years,—at the expiry of which period those bonds are to be paid off by the State. In return, the companies are to pay to the Government, as a first charge on their net profits, and by weekly or monthly instalments, the amount of the interest due upon those Government bonds, *plus* 1 per cent as a commission or profit on the transaction to the Government. For example, suppose that the present creditors of railway companies will accept State-bonds bearing $3\frac{1}{2}$ per cent interest, in lieu of railway-bonds (debentures) bearing $4\frac{1}{2}$ per cent interest: then the companies, in paying 1 per cent more to the State than the actual amount of interest which the State has to pay on its bonds, would pay no more than they would have to do if they issued bonds of their own, as at present. And even if those State-bonds—Railway Consols, in fact—would not float under 4 per cent, it is reasonable to hold that companies' bonds would not float under 5 per cent. So that, thus far, the companies which found it necessary to avail

themselves of this arrangement would be relieved of their present difficulty at no loss to themselves.

But what gain would it be to the State? In order to appreciate this part of the proposed plan, we must look forward to the end of the half-century over which those operations are to extend, and see what would then take place. During each year of the period, the State would receive from the railway companies 1 per cent more than it paid out to the holders of the debentures. And this 1 per cent, if invested in Consols, at the end of fifty years would, at compound interest, amount to the capital sum of those debentures. The State, it is true, would not make a net gain of 1 per cent on this operation: for the salaries of the new Government Auditors, and also of the new Office for the issue and supervision of the Government railway-bonds, would have to be deducted: but, for simplicity of statement, let us put this out of account. Let us also suppose that this plan were regarded as so favourable that all the present railway companies took advantage of it,—in other words, that the whole amount of existing railway-debentures, amounting to fully 100 millions, were thus transmuted into a Government debt: then, at the end of the half-century, the State would have become possessed of an amount of Consols equal in value to at least 100 millions sterling.

What is the best use which the State could make of this possession? The first idea which suggests itself is, that the State should simply cancel these 100 millions of Consols, and thereby reduce the National Debt to an equal amount. But this course is not included in Mr

Crawford's plan,—by which the State, while taking the whole debenture-debt of railways on its own shoulders, engages to pay off the capital sum at the end of fifty years. The 100 millions sterling, therefore, must be paid away to the debenture-holders. This the State would do, either by paying the debenture-holders in Consols (if they would accept payment in that form), or by gradually selling off Consols to that amount in the market, and paying off the debenture-holders with the proceeds. Thereby the State would take the place of those debenture-holders, and thenceforth would rank as first creditor against the railway companies for (say) $4\frac{1}{2}$ per cent interest on that amount,—*i. e.*, $4\frac{1}{2}$ millions sterling a-year. As we do not doubt that the railway companies would always be able to meet this annual payment to the State, the result would be that at the end of these fifty years the State would have £4,500,000 a-year at its free disposal,—to devote either to the reduction of the taxation of the country, or to the reduction of the National Debt.

II. But Mr Crawford proposes that the State should make a different use of the annual wealth so acquired. He proposes that the State should convert this annual gain of $4\frac{1}{2}$ millions (acquired at the end of fifty years) into a fund for the purchase of the railways. And in order to facilitate such a procedure, Mr Crawford proposes that all the railway companies which apply to the State to relieve them of their debenture-debt (on the above-mentioned terms) should agree to give the State possession of all the *land* occupied by or belonging to these railway companies gratis at the end of ninety-

nine years. Accordingly, while at the end of fifty years the State would hold in its own hands the whole present debenture-debt of the railway companies, deriving therefrom a revenue of 4 or 5 millions a-year; at the end of other fifty years, or a century from the present time, the State would also become possessed of all the *land* occupied by the railways,—from which, of course, it would thereafter derive an annual rent of a very considerable amount. Moreover (as the final object of all these transactions is to get the railways wholly into the possession of the State) Mr Crawford proposes that all the companies who avail themselves of this State-aid should likewise consent that the State should have the right to purchase the lines, at any time after the first half-century, at a valuation of the profits for the two years immediately preceding. And no doubt, what with the 4 or 5 millions of annual payments from the railways upon their debenture-debt (then wholly in the hands of the State), and also with the sum annually received as rent from the companies for the land which they occupy, the State would (*ex hypothesi*) have a surplus fund in hand equal to the gradual purchase of most of the existing lines. In this way, if all things went smoothly, the State might at the end of a century become possessed of all the existing railways, amounting in value to 400 millions; thereafter obtaining from the working of them a revenue of (say) 5 per cent, or 25 millions a-year: to be applied in any way it pleased,—in reduction either of railway-fares, or of the national taxation, or in the gradual extinction of the National Debt.

Now, let us consider this scheme *per se: i. e.*, irrespective of other modes which may be suggested for accomplishing the same object.

First, as regards the *Railways*. Consider the onerous nature of the terms to be imposed. The State is to demand (1) one per cent of profit on the transaction; (2) the cession of the land belonging to the companies; (3) the right to buy the lines at a price regulated by their average profits (at how many years' purchase Mr Crawford does not say) for any two previous years,—a right which naturally would be exercised at a time when the profits of the companies happened to be at the lowest. It can hardly be doubted that the acceptance of these terms by a railway company of ordinarily good position would diminish the value or market-price of its shares. No company, in fact, would avail itself of this proposed arrangement unless it were in difficulties. A railway company of ordinary repute could certainly float its debentures (especially if these bonds were for short periods, as at present) at one per cent above the rate of interest which the State could offer; and therefore it would not submit to the ulterior conditions of ceding its land gratis to the State, and of giving to the State a compulsory power of purchasing the line upon terms the least favourable to the company. Accordingly the probable result of Mr Crawford's plan is such as would fail to realise the expectations upon which the plan is advanced. The scheme would be accepted only by bad or temporarily embarrassed lines. And to get possession merely of such lines would be no adequate compensation for the State's engaging in this transac-

tion,—which, as we shall next show, would be a much more onerous affair than Mr Crawford imagines.

Secondly, as regards the *State*. To put the case in the most favourable form, let us suppose that every railway company in the kingdom is willing to adopt this proposed arrangement. What would be the gain to the State? We grant at once that there is no risk of any line being unable to pay to the State the stipulated rate of interest (whatever that might be) on its debentures. We cannot conceive any line being so unprofitable as not to be able to pay interest on its debentures: the only difficulty in the case of any company has been to *pay off* these bonds,—which is quite another affair. Therefore, we repeat, the risk which the State would encounter under such a scheme, in undertaking to pay interest on the railway-debentures, is practically *nil*. The second point to be noted is, that the State would not make a net profit of 1 per cent on these operations, seeing that the salaries of the new staff of Government officials requisite to carry out this arrangement would constitute a deduction from the gross profit of 1 per cent. The third point is, that these State-secured railway-bonds (Railway Consols, in fact) would enter into competition with the Funds as a mode of investment.

This is a most important point. In fact, the whole plan rests on the supposition that the public would prefer State-bonds for $3\frac{1}{2}$ or 4 per cent interest to railway-bonds for $4\frac{1}{2}$ or 5 per cent. As we have said, these State-secured railway-bonds would in fact be Consols, —with the speciality that a railway would be pledged as security for them, and also that the State binds itself

to pay off these bonds at par at a certain date. Hence they would be quite as good as Consols; so that the tendency of the scheme would be to depreciate the price of the Funds. For, be it noted, it is only a certain class of people who are willing to invest at 3 per cent. Although there is capital enough in the country to take up the whole amount of these new Railway Consols, it is not certain whether there would be enough of that *kind* of capital to do so. A large class of capitalists will not consent to invest at $3\frac{1}{2}$ or 4 per cent, seeing that they can get 10 per cent or more by investing their money in business. It is only reserve-wealth of non-traders that is invested in Consols,—and this amount of capital, although doubtless very large, is limited: and if ever that limit be reached (as has previously happened in our history), even the State itself must offer a high rate of interest for its loans.

But suppose that the reserve-wealth of the non-trading (or simply investing) portion of the community be sufficient to take up the 120 millions of railway-debentures at a low rate of interest—say $3\frac{1}{2}$ per cent—without depressing the price of the Funds. This would suffice for ordinary times. But, under an arrangement which is to spread over half-a-century at least, exceptional times must also be taken into account. Suppose, for example, that this country is involved in a great war. Then the Government must borrow largely—it may be for many years in succession. In this case it could not get the required loans at 3 per cent, or at anything like these terms. The amount of capital already invested in the Funds, with the new amount

invested in Railway Consols, would be quite equal to the total amount of that *kind* of reserve-wealth which it is possible for the State to borrow at a low rate of interest. Hence for its new loans the State would have to pay high rates (all the higher owing to the existence of these Railway Consols)—not owing to any diminution of its credit, but simply in consequence of the reservoir of capital from which such loans usually come (*i.e.*, from the non-trading community) being exhausted. Once that point is reached, we repeat, the Government must always pay dear for its loans. Instead of $3\frac{1}{8}$ per cent (the ordinary interest in the Funds), the Government may have to pay twice as much,—possibly 6 or $6\frac{1}{2}$ per cent.*

As regards merely fluctuations in the value of money on loan, Mr Crawford's plan, it is true, presents no difficulty: for if it were impossible for the Government to borrow money at 5 per cent, it would be equally impossible for railway companies to get loans at 6 per cent. Hence the Government could always fairly claim from the companies which acceded to this arrangement, the 1 per cent of profit or commission for securing

* This would be equivalent to a fall in Consols to 50! The rate of interest would remain nominally the same as at present—*i.e.*, 3 per cent,—but each subscriber to the loan would be credited with £200 of Consols for every £100 subscribed. It would be better, in such a case, to create a new Stock, bearing 6 per cent interest. The *amount* of interest payable on the National Debt would be the same in either case; but if the latter course were adopted, it would be much more easy, when peace returned, to pay off the debt so contracted. By paying £1000 we could extinguish an equal amount of Consols, on which we have to pay 6 per cent (£60,000); but it would require £2000 to extinguish an equal amount of interest payable on debt contracted the other way.

their debentures by a State-guarantee. But there would be no security at all against the rate of interest in these Railway Consols, and also upon the Funds, rising to a very high point, owing to the portion of the wealth of the country from which these cheap loans to the State are drawn becoming exhausted.

Accordingly two important deductions are justified by these considerations. First, as regards the companies. Since these proposed Railway Consols are only to be repayable at the end of half-a-century, the public, in subscribing the required amount, will take into account the exceptional periods when the value of loanable capital rises to a very high point, and will make their terms with the State accordingly. Secondly, as regards the State. If it were certain that the State would never require to borrow beyond the limits of the amount of reserve-wealth which the public is willing to invest in the Funds at the present rate of interest on these securities, all would be well. But it is to be feared that the addition of 120 millions to this kind of investment (by the creation of Railway Consols to that amount) would trench upon the future power of the Government to raise new loans at the present rate of interest payable on the Funds. So that, if the Government, in consequence of a great war, required to increase the National Debt to a considerable amount, the existence of those Railway Consols would constitute a necessity on the part of the State to offer a higher rate of interest on the new debt to be contracted than would otherwise be requisite. Hence, if the Government were to adopt Mr Crawford's plan, for the sake of obtaining possession of the rail-

ways a century hence, it might in the interval have to incur increased costs in connection with the National Debt, which would neutralise the contemplated gain,—even supposing that that gain were as real as Mr Crawford imagines.

In fine, we believe that the obstacles to the realisation of Mr Crawford's plan are insuperable. Under a system of government like ours, it is almost, we believe wholly, impracticable to establish a fixed policy which, in order to accomplish its object, must be maintained intact for a hundred years. The case of India, in this respect, furnishes no parallel. Apart from the vast difference in the relations between the railways and the State which exists in the two countries, it is to be remembered that the Indian Government can pursue any given policy with a fixity that is quite impossible here. In India there is virtually no public. The Government determines everything according to its own will. Whereas in this country, the Executive can do nothing without the assent of the National Representatives — a body which fluctuates from year to year, not only in its members, but still more in its opinions.

Other Plans.

Taking all these matters into consideration—paying regard alike to the probable refusal of the best railways to accede to the proposed terms, as well as to the difficulties on the part of the Government to undertake such a responsibility, and to carry out a series of operations extending over a century,—we believe that Mr Crawford's plan is actually less feasible than one which

should propose the immediate and direct purchase of the railways, or at least the trunk-lines, by the Government.

If such a plan were adopted, it would be impossible, of course, for the Government to make the purchase by a single payment of vast amount. But such a course would not be necessary. It would not be necessary to pay the capitalised value of the railways. As Government bonds would be quite as realisable as railway-shares, the Government might purchase the railways simply by agreeing to pay to the shareholders *in perpetuo* an annual dividend fully equal to the present amount of their profits; and it would have to trust to obtain an equal sum from the revenue of the lines. As regards some of the great lines—the London, Chatham, and Dover, Great Eastern, &c.,—we believe such a transaction could be made *now* on good terms; though even in these cases the shareholders would ask for more than they are now getting. On good lines, again, like the Great Northern, the company could fairly claim a much higher rate of dividend than at present. The consequence would be that, at the outset at least, the Government would either have to increase the National Debt, or raise the amount of the taxation. The country would not stand the latter course; nor, indeed, would they stand the former either. They would not think the game worth the candle. The Government could hardly manage a line better, more efficiently and economically, than a Board of Directors, directly interested in the profits of the line. Nor would the public desire that the political influence of the Government should be strengthened by so great an addition of patronage thus placed at its disposal.

General Objections.

Moreover, in no case is it possible to conceive that the State would desire to obtain possession of *all* the railways in the country. Whatever arguments may be advanced in support of the purchase of railways by the State, these arguments (whatever be their worth) can only apply to the purchase of the great trunk-lines of the country. It would not be an easy matter to dissociate those trunk-lines from the branch-lines in the hands of the same companies. At all events, if the State, in dealing with the companies, is to be allowed to pick and choose—in other words, to take from the companies simply those parts of their property which it best suits the State to acquire,—it is needless to say that the State would have to pay a much higher price for those selected lines than if it were to purchase the entire property of any great railway company. The company would be totally disorganised; and in many cases the shareholders would doubtless refuse point-blank to work the mere fragments of their property so left to them. In truth, then, the State would have to buy the whole property of a company, and thereafter endeavour, as it best could, to re-sell those branch-lines the working of which it did not choose to undertake.

But, it may be said, after obtaining possession of the lines, the Government might lease some of them. Well, but what profit would there be in that? If the State acquired the lines at their fair value, it could gain nothing by merely leasing a line to a new company. The rent or revenue which it received would only equal the

interest on the money which it has paid for the line,—*i.e.*, the dividend which it has engaged to pay *in perpetuo* to the previous owners of the line.

An important objection of a different kind still remains to be considered. Apart from the formidable difficulties in the way of the State obtaining possession of the railways, and apart also from the doubt as to whether the State could work the railways as efficiently as the present companies, there remains in reserve the important fact that if the State were to purchase any or all of the existing lines, it would thereafter have a direct interest in preventing the construction of new lines which might in any degree enter into traffic-competition with the existing lines, and thereby tend to diminish the profits on those lines,—which profits would be needed to enable the State to work the lines without drawing upon the public purse. If the State were thus to impede the construction of new lines, the result would be most injurious to the development of the national industry. In fact every year of delay thus occasioned in the construction of new lines by the obstructive policy of the State would constitute a serious negative loss to the country, —it would obstruct the increase alike of industry, of wealth, and of employment.

Accordingly, as the upshot of the whole matter, we see nothing for it but to let the railways remain private property as at present. The Government does not make roads; and yet roads, and costly bridges to boot, are made most efficiently without its aid. Why, then, cannot the construction of railways be left equally in the

hands of the public,—especially as railways, unlike roads, are a field for private speculative enterprise?

We acknowledge that requirements of State-policy might possibly arise adequate to justify the Government in purchasing certain railways,—for example, it may be, the Irish railways. But the consideration of such questions is beyond our province. Financially—and also as a matter of principle—we hold that it is much better alike for the State and for the public, that the Government should not trade in railway property, but that railway enterprise should be left, as at present, to private enterprise and speculation.

Moreover, if the State is to interfere at all with railway-works in Ireland, it ought to do so not by purchasing the existing lines, but by aiding the construction of new ones. Railways are a most important adjuvant of Production; and, upon national grounds, we think the State ought to assist by this means the development of the resources of the sister-isle, where private enterprise is inadequate for the work. The State might either construct those new lines itself, or, still better, it might give a guarantee of 5 per cent interest on the cost of their construction. These new lines would act as feeders to the existing ones: so that the present railway companies would be benefited, while a vast boon is conferred upon Ireland at large.

XXVII.

RAILWAY FINANCE

A SAD collapse has fallen upon railway companies and railway enterprise. Some of the greatest railway companies have come to grief: and if any new railway project were to be launched, it would be laughed out of the Stock Exchange. Nor is it easy to say, so long as railway enterprise is conducted upon its present footing, when a change is to be looked for in this unpleasant state of matters. In course of time, we doubt not, all the existing lines will become remunerative enterprises. But it will take a still longer time before capital is freely invested in the construction of *new* lines. Yet, new lines must be constructed. It will never do for railway enterprise to stand still. Railways are an indispensable element in the progress of a country: they cheapen production, the mainstay of a nation's wellbeing; and at the same time they add greatly to the amenities and social comforts of life by accelerating locomotion, and enabling individuals at a distance from

one another to maintain the home and social ties as if they were but a few miles apart.

The work of railway-construction must and will go on. But, in order that it may do so, we must eliminate from railway enterprise some of the obstacles which recently have proved so disastrous to the existing lines; and also, in many cases, recourse must be had to other systems than that of public companies of the kind now in use.

Faults in the Past.

The chief evils of the present system may be classed under three heads. Firstly, railways have hitherto paid too much for the land which it has been necessary for them to purchase in order to construct their lines,—and also too much in the form of Parliamentary expenses. Secondly, there has been financial mismanagement. Thirdly, there has been over-competition among the railway companies.

When railways first came into use, landowners, in most instances, looked upon them simply as nuisances —as things necessary (it might be) for the trade of the country, but of no use to the land, and greatly destructive to the amenities of their estates. The "amenities" constituted a heavy item in the prices which companies had to pay for the land. Nevertheless, what appears an ugliness in one form of civilisation may become an object of interest, as well as of utility, after a new system has come into use; and nowadays, the charge for loss of amenities has almost entirely disappeared. The benefit of railways is now so fully acknowledged

that landowners, instead of obstructing them, are only too glad to have lines passing through their estates. The exorbitant Parliamentary expenses, which have absorbed so much of the capital of railway companies, were to some extent occasioned by the obstruction offered by the landowners, but still more by the rivalry of the companies,—each opposing the other's Bill in the hope of excluding a competitor from the field. Probably a less costly method of conducting such Parliamentary inquiries might be adopted: but in the main the waste of capital in such conflicts has been occasioned by the two causes above mentioned.

These are, comparatively, faults of the past. What is most important is to consider the two other defects of our present railway-system:—

(1) As to *Financial Mismanagement.* This has arisen mainly, though not exclusively, in connection with the third-named defect of the present system—namely, over-competition. The companies, from this cause, have been led to embark in extensions of their lines, which they had not sufficient capital of themselves to construct; and, in consequence, rather than be outdone by rival companies, they have invoked the financial aid of the large railway-contractors. These contractors, of late years, have mainly supplied the finances by which the new lines were constructed, and by which they themselves were paid. The companies could not do without them, and naturally they exacted exorbitant terms. Such exorbitant charges are natural enough, looking to the great risk which the contractors undertake. In good times it makes them rich men,—

they amass enormous fortunes almost in a couple of years; on the other hand (as has been seen lately) in bad times they come to the ground, and are reduced from millionaires to bankrupts.

We do not depreciate the aid which contractors have afforded to railway enterprise. What are called "contractors' lines" constitute, doubtless, a very risky kind of business: they only succeed in fair-weather times; any monetary crisis at once brings them to the ground. Nevertheless, risky business is an essential feature of a rapidly progressive country like ours. It exists in every branch of trade, from the little shopkeeper up to the largest manufacturer or wholesale dealer. And in railway enterprise much has been accomplished by the help of those contractors (many of them large capitalists) which could not otherwise have been achieved. If a line can be constructed by means of capital fully subscribed by the public, the work can be done at much less cost than if the company has to invoke the financial aid of a contractor. Nevertheless, much may be done by credit alone; and contractors are willing to aid largely in the construction of lines, in order to obtain employment for themselves. By their help, railways have been constructed which could not have been undertaken for years if the entire capital had to be obtained from the public. And in this way the country has been greatly benefited.

But in many cases there has been a heavy loss to the railway shareholders. The companies take loans (so to speak) from the contractors only when they cannot raise the sum from the public, in the shape of new shares or

preference-stock. And the contractors, on their part, naturally exact an exorbitant rate of pay for their work, as well as for their financial services to the company. Hence a railway constructed by such help always costs one-fourth, and sometimes even one-half, more than if the capital had been raised in the usual way,—*i. e.*, from the public, in the shape of shares. Part of this loss is borne by the country, which has to pay higher charges to the company for railway-travelling than would otherwise be necessary. But the main loss falls upon the shareholders: for it is very difficult for a company to raise its charges above the usual rate, owing to the keen competition for traffic, and the fear lest a portion of its business should be driven off to a rival line.

(2) As to *Over-competition.* This, we have said, has been the main cause of the recourse of railway companies of late years to the financial aid of contractors. They have been forced, or have fancied themselves forced, to undertake more works than their own capital was equal to. We believe that all the lines thus executed under the pressure of competition were fitted to prove remunerative, but for the exorbitant terms which the companies undertook to pay to the contractors. It is not that the lines are bad—bad at least in the long-run: it is the exorbitant terms of construction which are the grand drawback upon them.

Competition can hardly be prevented: and it is not desirable that it should be prevented, otherwise than by the influence of prudential considerations upon the companies which are prone to engage in it. Every

main line of railway hitherto constructed would at this moment be yielding vast profits, if (as was expected by its projectors) it had remained without a rival in its own field. But what happened was this. Either some new company was started, to make a more direct line between the same terminal points ; or else some neighbouring line threw out branches so as to "tap" the traffic, and acquire for itself a portion of the trade of its rival. In the former case, the rival lines had to compete with one another by a reduction of their fares, —each seeking to drive the other out of the field, and to establish itself as exclusive possessor of the "through" traffic ; in the second case, each of the two rival companies sought to take possession of the neutral district which lay between them, and, by means of branch-lines, to drain the traffic of that district into its own main line.

In a level and populous district like the south of England, such competition has full play. In a hilly country, like the north of England, and still more in Scotland, it is greatly restricted by the geographical features of the country. But in Scotland the competition has assumed a new form. Owing to the fact that there is hardly any wide extent of plain—each line of railway having (speaking roundly) to run in its own valley, or series of valleys,—there has been no great construction of rival lines in Scotland ; but the spirit of rivalry exists all the same, though in a new form. *There* it displays itself, not by the construction of new lines, but by one or other of the larger companies buying up the small ones, so as get for itself an outlet not equally open to

its rival. So circumstanced, it can throw obstacles in the way of all goods or passengers which leave this outlet or terminus by the other line, while of course its own goods or passengers are passed on with special despatch. In this way it seeks to obtain for itself the "through" traffic to this point which previously passed over the rival line.

This, for example, has been the form taken by the rivalry of the two great Scottish railway companies, the Caledonian and North British. The original terminus of the North British was at Edinburgh,—that of the Caledonian at Glasgow. But when the rivalry between those companies reached its height, each sought to gain possession of the other railways which led northwards from those points. It is obvious that if either of those companies had obtained possession of the lines (there are only two) leading northwards from Edinburgh and Glasgow, it might thereby, by obstructing the transit of its rival's goods at those points, have obtained for its own main line the whole traffic from England which was meant to proceed northwards beyond Edinburgh and Glasgow. In this fierce rivalry the North British has been the most daring; but its efforts far exceeded its resources, and so, in the very hour of its apparent triumph, it suddenly came to the ground,—while its rival, whose efforts were less in excess of its resources, goes on, though not flourishingly, at least with some measure of success. What the issue might have been if the capital of the North British had been equal to its enterprise, it is hard to say. But the lesson is the same in this case as in that of railway competition in the south.

of England,—namely, that the spirit of rivalry has tempted railways into an extension of business far exceeding what their capital justified; and consequently, on the advent of difficult times, those ambitious schemes have collapsed before they could bear fruit, and the railways which undertook them have fallen into a state of serious embarrassment.

After the sharp lessons thus received, there is probably little danger of a revival of this system of over-competition. It is more likely that henceforth the rival companies will seek to combine, and form Federations extending over large areas of the kingdom. This is a better course for them than to continue the system of reckless competition. But it will require to be most jealously watched by Parliament, in order to protect the interests of the public. Any Acts passed for the federation of railway companies ought to be made renewable in a few years, so that an efficient check may be kept on any abuse of this virtual Monopoly of the traffic of the country.

Present Difficulties.

The grand difficulty in railway finance, as recent experience has plainly shown, arises in connection with the Debenture-debt: that is to say, it is owing to the manner in which the companies raise the borrowed capital which is necessary to carry on their operations. Every large railway company has obtained authority, by Act of Parliament, to raise loans to an amount equal to a fixed proportion of its paid-up capital, and has fully availed itself of this power. In this way it can

carry on its operations to a larger extent than its own capital enables it to do; and in so far as this borrowed capital can be employed at a profit, the arrangement is very advantageous to the companies. But this borrowed capital is permanently invested in the works or business of the companies, so that they cannot possibly do without it. If this borrowed capital were withdrawn, the railway companies would at once be brought to a standstill. They could not carry on their operations; they would become bankrupt.

What, then, is the form in which this borrowed capital is raised by railway companies? As every one knows, it is raised in the form of Debentures,—railway-bonds issued for four or five years, and payable at the end of that period. Every debenture-holder—*i.e.*, every one who has lent money to a company upon such bonds—is entitled to demand repayment of the loan at the end of (say) five years. The debenture-holders may renew their loan, by taking other debentures current for other five years, or they may not,—they may demand repayment. But, if they decline to renew these bonds, the railway must of sheer necessity get other parties to take new debentures equal in amount to those which have expired,—in order, with the money thus received, to pay off the previous debentures. This is imperative. If a company cannot do this, it has no money with which to discharge the expired loans, and so must become bankrupt.

Obviously this is a serious liability. In fair-weather times, it is true, no difficulty is usually experienced; for, if some debenture-holders decline to renew their

loans, there is no lack of other persons who are willing to do so; so that, in ordinary times, this borrowed capital creates no difficulty for railway companies. They can always pay the interest on it: and thus, so long as these debentures can be renewed, all goes smoothly. But, unfortunately, the fair-weather of our money-market is ever and anon seriously disturbed,—occasionally, it is broken by hurricanes which sweep away the credit even of thoroughly solvent firms and companies.

Loud complaints have been made against the Parliamentary enactment that the debentures (representing the borrowed capital) of railway companies should run only for comparatively short periods. But this was really no hardship. But for this condition, the public would not have lent its reserve-wealth to the railway companies upon equally favourable terms: indeed, it is doubtful if money would have been lent upon any terms for long periods to the railway companies to the amount required by them. The value of money on loan varies from time to time: hence it is for the advantage alike of the companies and of the public that the rate of interest on the loans should be revised at stated intervals. If the debentures of a company expire at a time when money on loan is cheap—*i.e.*, when the bank-rate is low,—the companies reap the advantage; if the debentures expire when the bank-rate is high, it is only right that the renewal of the debentures should be made at a higher rate of interest than before. The present system, therefore—*i.e.*, if the companies are to borrow at all—is so far perfectly wise

and just: it is mutually advantageous alike for the companies and for the public.

Nevertheless the defects of this system are most serious. What happens when a great monetary crisis occurs, — a calamity which, under our present bad monetary laws, has thrice befallen the country during the last twenty years? For example, what took place during the Crisis of last year? For more than three months the *minimum* bank-rate was 10 per cent; and for a portion of that time, it was impossible to get loans upon any terms, except upon the best and shortest-dated securities. Of course, at such a time, some of the railway companies found it impossible to obtain a renewal of their debentures. Accordingly, it is from the Crisis of last year that the grand difficulty which now besets railway companies dates its origin. Several railway companies whose debentures then fell due, could not get them renewed. In consequence, they became insolvent. No railway company, however prosperous, can at once pay off its debentures (*i.e.*, the amount of its borrowed capital, which it has permanently invested in its works); accordingly when, owing to the Crisis, several companies could not obtain a renewal of their debentures, a widespread disaster overtook our railway system. The credit of many companies at once disappeared: they became insolvent concerns, which the public thereafter would not trust.

Doubtless there has been much railway mismanagement, yet there is not a single railway company which is not in a position to pay the *interest* on its borrowed capital. There may be no dividend for the shareholders,

but at least there are ample means for paying the interest on the debentures. And as long as a company can pay its current liabilities, its credit remains good. But the Crisis of 1866, by rendering it impossible for the companies to obtain a renewal of their debentures, imposed upon them a difficulty which no company can meet—namely, the immediate repayment of its borrowed capital. And, simply in consequence of this impossible task being thus laid upon certain companies, the credit of those companies received a shock from which it will take years to recover. Hence, while fully acknowledging the mismanagement of many railway companies, we repeat that it was the Crisis of last year which has been the main cause of their present difficulties, by imposing upon them the necessity for "cashing-up" which no railway company is adequate to meet, and which would not have arisen but for the terribly severe and highly exceptional monetary difficulties which marked the Crisis of 1866.

The practical point, then, is—How is this weak point in our railway finance to be remedied, removed? To give the railway companies the power to issue their debentures (the bonds by which they raise the large borrowed portion of their working capital) for longer periods than at present, would do no good. The companies which at present cannot get their loans renewed for periods of five years, would find this difficulty increased, if they were to attempt to float their debentures for a longer period. Obviously some other plan than this must be devised.

At present, there exists a twofold drawback upon the credit of railway companies. (1) There is no adequate

security for the repayment of railway-bonds when they fall due; (2) nor is there even a means of insuring the genuineness of the statement of accounts which railway companies submit to the public. If there were an adequate security for the payment of debentures when they fall due, it would be of no consequence to the lending public whether the published balance-sheets of the companies were correct or not. But, seeing that there is no such security for the repayment of these loans, the only means by which the public can judge of the power of a company to meet its engagements is the half-yearly statement of its accounts submitted to its shareholders. And such statements of accounts, as is now painfully evident, cannot be relied on.

REMEDIES.

It is a matter of vast importance to obtain a remedy for these defects, and to devise a means by which Railway credit may be established on a solid and permanent basis. For it is a great mistake to suppose the Age of Railways is past. Railways have a vast future before them. They will yet extend over the whole country, till every rural valley has its little line, and till steam-power supplements horse-traction on every highway. When such is the expansion which our railway-system is destined to experience, it is a matter of paramount importance that the credit of railway companies—in other words, the negotiability of their bonds and debentures—should assume a more solid form, in order that

those securities should take a suitable place in the general credit-system of the country. Already the amount of these railway-bonds is fully 120 millions (besides the share-certificates, amounting to about 400 millions); and in process of time they will amount to a still vaster sum—constituting, next to the Funds, the greatest field of investment for the reserve-wealth of the community.

The remedy, like the difficulty to be overcome, may assume a twofold shape: namely, (1) it may consist either in obtaining an adequate guarantee for the debenture-debt of railway companies, or (2) by insuring a periodical statement of their accounts of so clear, full, and *reliable* a character that the public can at all times be able to judge correctly of the financial condition of those companies.

The first and most important point to be determined is, whether it is possible to obtain an adequate guarantee —a guarantee given by some other party than a railway company itself—for the payments in connection with railway-debentures. If this can be obtained, no more is needed. But can it be obtained?—and how?

In these times, when State-intervention seems to be regarded as the great remedy for all defects in our financial system, the first remedy thought of is, a State-guarantee for railway-debentures. But such a proposal is out of the question. Even when suggested as a means of enabling the State thereafter to obtain possession of the railways (as a part of Mr Crawford's grand scheme), it met with little support in Parliament; and Mr Crawford himself has repudiated the

idea of countenancing such a State-guarantee *per se*,—*i.e.*, save as a means of obtaining for the State a great prospective advantage. If, then, an adequate (and therefore *extraneous*) guarantee of railway-debentures can be obtained, it must be through the instrumentality of private enterprise. How is this to be done?

Railway-Securities Companies.

The proposal of Mr Crawford, in connection with his great scheme for the purchase of the railways by the State, was, that the State should guarantee the regular payment of railway-bonds, charging a commission on the transaction. The State was to take up the debenture-bonds of railways, and re-issue them (virtually in the form of Railway Consols) to the public at a lower rate of interest: the railway companies paying to the State (say) 5 per cent interest on their debentures, and the State issuing bonds of its own to the public for the same amount at 4 per cent,—giving the State a gross profit of 1 per cent on the transaction. This is a very high commission (equal to 25 per cent): obviously such a guarantee or insurance business would *pay* at a much lower rate of commission,—in other words, if a private Company were to undertake the guarantee, it could profitably offer its bonds to the public at $4\frac{1}{2}$ per cent (instead of the 4 per cent offered by the State), while receiving 5 per cent from the railway companies. Accordingly the question suggests itself, Cannot an adequate guarantee be obtained without the intervention of the State? Cannot private enterprise accomplish the object of imparting to railway-

bonds an adequate security, and thereby entitle them to take their rightful place in the general credit-system of the country?

It seems a great marvel that the bonds of private traders, of whose affairs the general public know nothing, should be amongst the most negotiable of all securities—should be readily convertible into money at their full value,—whereas no equal, or nearly equal, negotiability attaches to the bonds (debentures) of great joint-stock companies like railways, which periodically publish a full statement of their financial condition. Is it not a marvel that the bill of a private merchant or shopkeeper should be readily convertible into money at its full value, whereas railway-bonds will not be advanced upon save to only two-thirds of their market-value? This fact shows unmistakably to what a small extent Railway credit has as yet been developed in comparison with Commercial credit. For there is certainly no natural reason why the bonds of railway companies should not be at least as negotiable as the bills of a private trader.

Partly, it is true, this difference is at present occasioned by the state of the law. A bill entitles the holder of it to obtain payment by a summary process from the person who has issued it; whereas a debenture-holder, as a matter of fact, has no means of enforcing immediate payment. Yet we doubt whether any insuperable difficulty exists in the way of making the claims of debenture-holders as enforceable as those of a bill-holder. Railway companies have not only no reason to object to such an alteration in the law, but, if they

take a right view of their interests, they, above all other parties, have a motive for desiring it. The more perfect the security they can offer, the lower will be the rate at which they can get the loans which they require. We think, then, that this is a reform which the law-officers of the Crown should set themselves to consider. It is not necessary that the process of recovering payment of a railway-debenture should be the same as that of recovering payment of a bill: the means may vary, but the end should be the same. And we think that a Lord Chancellor or an Attorney-General would most usefully employ his legal acumen in radically examining the case, and, if possible, in removing the difficulties which at present stand in the way of this reform.

Nevertheless, even with the law as it stands, much may be done to place Railway credit on nearly the same good footing as Commercial credit. How is it, in fact, that the bill of a private trader is so readily convertible at its full value into money? Because a whole class of financial establishments have been created for the purpose. Banks and discount-houses are the instruments by which this process is effected. A trader or shopkeeper cannot get loans from the general public, as railway companies do: the general public will not look at his bills,—they are only accepted by a few persons who are, or who believe themselves to be, acquainted with his circumstances. How is it, then, that such private bills are so readily convertible into money? Simply because banks and discount-houses make it their special business to deal in such securities. These

establishments are, as it were, a market where commercial bills are bought at their full value.

Railway securities are of yesterday, — they have sprung into existence within the last quarter of a century. And as yet, they have not been brought within the pale of our financial system,—that vast fabric of Credit which is the offspring of mature civilisation, and the greatest marvel of our times. But, sooner or later, they will be brought within the pale. Of that we feel assured. Our purpose is simply to hasten that desirable consummation. How, then, is this to be done? It must be accomplished by a process similar to that by which commercial credit has been developed by means of Banking. Let us, in a word, explain the process:—

A bank-manager's chief ability is displayed in knowing a good bill (or other security) from a bad one. The most important functions of a bank or a discount-house consist in the *valuation of securities,* and in the conversion of these securities into the most negotiable form — namely, Banking-currency, or bank-notes and cheques convertible into coin on demand. In *essence,* the process is this: that a bank endorses with its name and credit the bills brought to it, and thereby renders them negotiable with the public at large. The bank interposes its own credit between that of the merchant and the community, and by this guarantee renders the merchant's bills generally negotiable. This is the *essence* of the transaction, though not the form. The form is, that the bank gives its own currency (notes and cheques) in exchange for commercial currency (bills),— charging a commission for the trouble which it takes

and the risk which it incurs. But in essence, the process is the same as if the bank, for a suitable consideration, took a merchant's bill, endorsed it or stamped it with its own name, and cut it up into small pieces so as to make it suitable for *general currency:* by which process the negotiability of the bill is vastly increased—firstly, because the value of the security is guaranteed; and secondly, because the security is converted into a form which makes it more available for general use.

Or take the more directly apposite case of a Land-Securities Company—(a kind of financial establishment unfortunately still rare in this country). The special function of such a company is (1) to guarantee the value of land-securities; and (2) to convert them into a more negotiable form. For example, when a land-bond, or mortgage on an estate, is brought to it, the company investigates the legal validity of the document, and also ascertains if the estate is so valuable that, if brought to a "forced sale," it would certainly realise the amount of the mortgage-bond. Having assured itself upon these points, the company takes the mortgage into its own hands, and gives in exchange for it the bonds of the company — which to some extent correspond to the notes of a bank. A simple mortgage is not a security upon which banks will make advances to its full value: but the bonds of a Land Company are readily negotiable by banks. Such bonds are issued on the security of the mortgage, after a careful investigation of its legal validity and of its monetary value; and their payment is assured alike by the value of the estate upon which the mortgage is held, and by the capital (or guarantee-fund)

of the company. The effect in this case is substantially the same as in banking,—namely, the validity of securities is guaranteed, and they are converted into a form more negotiable than they originally possessed.

Cannot the same principle be applied to railway-debentures? At present the amount of railway-debentures always afloat is reckoned at fully 120 millions sterling, a sum equal to the total amount of commercial bills afloat forty years ago,—the discounting or negotiation of which bills furnished the chief business of the banks of that time. The public, accordingly, has a remedy for the present difficulty in its own hands. A Railway-Securities Company, or several of them, is the best as well as the most natural remedy. Such companies, by their guarantee-fund or capital, would at once give the desired validity to railway securities. And, secondly—though this is apart from the present question,—these companies could add another element of value to such securities, and also increase their own profits, by issuing in exchange their own bonds for smaller sums. For example, in exchange for a railway-debenture for £600, they might issue thirty bonds of their own for £20 each, or even smaller sums,—current for short periods, and bearing interest.

Such a system would not fail to attract more capital for the railways than otherwise they could obtain. Moreover, if such a system were established, the bonds issued by those Railway-Securities Companies would be readily purchased, as short investments, by the class of small capitalists, who, for want of suitable investments, at present keep their little reserves in the sav-

ings-banks or ordinary banks. We may add that this class of capitalists are of all others the most deserving of having their wants attended to, in order that as large a portion as possible of the humbler classes may be led to cultivate economy, and thereby gradually raise themselves into a more permanent condition of well-being.

Such a scheme, it is true, belongs to the future. In the present state of affairs it may appear less practicable than we believe it to be. Like most proposals of reform, it cannot be rightly judged simply by the present condition of things. Our financial system—the fabric of Credit upon which our industrial greatness rests—is yearly extending. Its beneficent operations are being gradually applied to various kinds of property and of industrial enterprise which hitherto have hardly been brought within its scope. The last few years have witnessed the establishment of Financial Companies, extending the joint-stock credit-system to many kinds of enterprise which cannot properly be included within the operations of banks and discount-houses. And although some of those new establishments have started badly, this is no more than was to be expected of the initial stage of any new kind of business; and, moreover, they have been subjected to a terrible monetary crisis, the effects of which have been unduly to depreciate the value of property and enterprise of all kinds, converting a great deal of good business into bad. Insurance companies, also—which are nothing else than guarantee companies, establishments which upon certain terms undertake to guarantee certain payments—have now

very widely extended their operations. Some of these companies guarantee individuals even against the pecuniary loss (so to call it) arising from accidents of all kinds. Others are ready to guarantee even the moral character of their subscribers: in other words, in return for receiving an annual sum from their subscribers, they guarantee to the employers of those men any loss produced by moral delinquency (such as embezzlement or other defalcation of accounts) on the part of any of those employés.

Since the guarantee system has already been carried to this extent, it is needless to say that its application to railway finance may be confidently looked for ere long. Nevertheless, let us put aside this proposal for the establishment of Railway-Securities Companies, and consider what other means are available for improving the credit of railway companies.

Improved Form of Borrowing.

The weakest point of railway finance, as we have said, is the Debentures. Every railway company has a debt of this kind,—and a worse form of contracting debt it is impossible to imagine. This debt is meant to be permanent,—the companies cannot pay it off,—yet every four or five years it is liable to be called up! It is needless to comment on the inconsistency of such an arrangement, or on the disasters to which the companies are thereby rendered liable. Obviously the companies ought either (1) to pay off this permanent debt; or else (2) they ought to free themselves from the ever-recur-

ring liability of being called upon to repay it when they know they cannot do so.

(1) By the aid of Railway-Securities Companies the railways might possibly convert their short-dated debentures into a Debt (Railway Consols, in fact) upon which of course they would have to pay the stipulated interest, but the capital amount of which they could not be called upon to repay. However this might be, certainly the unaided credit of the companies is not sufficient to induce the public to assent to such an arrangement. Even if the debenture-debt were contracted for longer periods than at present, the companies would have to pay a higher rate of interest on it; and, moreover, it is doubtful if even a higher rate of interest would tempt the public to lend the money to the companies upon such terms.

(2) But why should not this debenture-debt be paid off altogether? Why should not this portion of the working-capital of the companies be transmuted into a better form of obligation? The holders of these debentures are persons who do not desire to speculate; so that it is needless to try to convert them into ordinary shareholders. But we do not see any insuperable obstacle to transmuting these debentures into Preference-shares,—into bonds (by whatever name they may be called) the capital amount of which is not repayable, but which bear a fixed rate of interest constituting a first charge upon the profits of the companies. It is true that some companies have so over-stretched their credit—by the issue of "Preference," "Pre-preference," and "Guaranteed" stock—that the holders even of those

privileged bonds cannot rely upon punctual payment. But this conversion of debentures into a really "Preference-stock" would not be liable to any such defect. It is the repayment of these debentures, in fact, which sometimes occasions the inability of the companies to pay the stipulated interest on their so-called "preference-shares." Now, as a matter of fact, there is not a single railway the net profits of which do not amply suffice to pay the interest on its debenture-debt; and if this debt were converted into a really preference-stock—constituting a first claim upon the revenues of the companies—the owners or holders of this debt would be better assured of punctual payment than they are at present. Of course, in such a case, the companies must bind themselves to issue no more floating debt—no new debentures in lieu of those transmuted into preference-shares; so that the transmuted bonds should under all circumstances constitute a first charge upon their revenues. The effects of such a change would be a great relief to railway companies: and we think, in order to attain it, it would be worth while for the companies even to offer a higher rate of interest (if this be necessary) upon the converted bonds than they pay on the present debentures.

Improved Form of Accounts.

Lastly, let us consider how the defects of railway credit may be remedied simply by an improved system of stating and auditing the accounts of the companies. This reform would greatly facilitate the adoption of either of the above-suggested remedial plans, but it is

so important of itself as almost *per se* to offer a solution of the present difficulties.

In order that this reform be effectual, two main points must be attended to. I. The Form in which the accounts are made up. II. A security that the statements included in those accounts are correct.

I. As regards the Form of accounts. The special requirements are, that the form in which the accounts are made up shall be clear and intelligible; and also that a uniform system shall be adopted by all the companies in the making up of their accounts.

The importance of uniformity in the accounts is self-evident. Unless every company make up its statement of accounts in the same form, it will be difficult for the public to ascertain the relative financial position of the various companies. There are no insuperable difficulties to the adoption of such an arrangement, and its advantages are manifest. Doubtless, in order to its attainment, much care must be bestowed on devising a proper mode, or form of balance-sheet; and in such a matter the leading men connected with railways must be amply consulted. Doubtless, also, it will be advisable that such an arrangement be effected under an Act of Parliament; in which case the final decision upon the various and conflicting proposals of the railway companies will rest with the Board of Trade.

In framing such a model balance-sheet, several important points must be kept in view. There must be a clear definition as to what is to be included under the head of "Working-expenses"—at present an item of very variable character. Also there must be a distinct

separation between the expenditure requisite to maintain the lines in their ordinary state of efficiency (that is to say, the cost of replacing the annual wear of the rolling-stock and permanent-way), and the expenditure which is a veritable outlay (either in the shape of "extensions," or of new engines and carriages) for the purpose of getting new traffic and additional receipts.

Let us consider these matters in detail. Take the case of a railway which has just been constructed, and supplied with all the rolling-stock (*i. e.*, engines, carriages, and trucks) required to carry on the estimated amount of traffic, which, we shall suppose, is exactly equal to the preparations made for its conveyance.

Then, every year both the "permanent-way" and the rolling-stock become deteriorated, and depreciated in value, by wear. So that, after a certain number of years, the rails and sleepers have to be replaced by new ones, and new engines and carriages have to be bought to replace the old ones. The period of endurance of those various parts of a railway varies, of course, with the amount of traffic, and in some degree also with the gradients and other circumstances. But under given circumstances, the period of endurance for the rails, carriages, &c., is easily calculable,—much more so than the endurance of individual life, which forms the basis of the calculations and business of a Life-insurance company.

A Reserve-Fund.

This fact really determines what ought to be the course pursued by railway companies on this point. A railway company, on its first starting, should no more

divide its full profits than a life-insurance company should do so. As every one knows, the annual profits of a life-insurance company are much greater, in proportion to the number of insurances, in the first years of its existence than they are afterwards,—seeing that several years must elapse before the deaths come up to the average rate of mortality. In like manner, in proportion to its amount of traffic, the profits of a railway company are much greater in its initial years than at the later period when the wearing out (the deaths, so to speak) of the individual parts of its property comes into operation. A life-insurance company, at its outset, lays-by a portion of its profits as a reserve-fund to meet the inevitably larger expenditure which it must incur in subsequent years. A railway company ought to act on the same principle. A portion of the profits in the first years ought to be set apart as a Reserve-fund, to meet the certain and serious additional charges which will arise when its permanent-way and rolling-stock are worn out. This reserve-fund ought to be no greater than is requisite to meet this replacement of property. When such replacement becomes necessary, the amount of the reserve-fund should be used for this purpose. And thereafter a new reserve-fund should be gradually established by small deductions from the annual profits, to meet the next replacements of the property, until the period is reached when the yearly replacements for each year will correspond with the average rate of mortality of the materials.*

* See Appendix.

Working-Expenses.

Secondly, as to annual repairs. Although most of these repairs really take the form of replacements, yet, to a certain extent, they must be treated separately. It is true, for example, that at stations and particular parts of the line where the wear is exceptionally great, the annual repairs consist in actual replacements of the rails by new ones. But these annual replacements do not in any way obviate the necessity for a renewal of the whole line, or permanent-way, at the given period. Say, merely in illustration, that the rails at stations have to be replaced yearly, while the rails on all the other extent of the line need only to be replaced every ten years: then, it is evident that the entire replacement of the rails along the whole line will be necessary every tenth year, despite the annual renewal of the rails at the places of exceptional wear. Accordingly, while the cost of renewing the permanent-way at distant intervals ought to be met by the establishment of a Reserve-fund, these annual renewals of small parts of the line ought, under all circumstances, to be included in the annual Working-expenses.

Other kinds of repairs ought to be similarly treated,—such as the breaking of the axles of the engines, the wear of the seats and lining of the carriages, &c. These (so to speak) prolong the life of the engines and carriages, but they cannot avert their ultimate death. A period comes when, despite these annual repairs, new engines and carriages must be purchased to replace the

old ones. Such details, however, may more appropriately be considered in the Appendix.

But there is another class of expenditure, the mode of meeting which cannot rigidly be determined. For example, suppose a great flood (unusual in this country, but common in India) destroys a large part of the line; or a great fire makes havoc in the terminal buildings of the line; or some terrible collision or other catastrophe not only destroys a portion of the rolling-stock, but subjects the company to heavy damages. In each and all of these cases the expenditure will not necessarily fall to be included in the working-expenses of the particular year. Only a portion of it may be so included, while the remainder is spread over several years. These cases, in fact, are accidents,—they are losses which, on the average, only happen once in so many years: and hence the loss arising from these accidents, instead of being deducted entirely from the profits of the particular year in which they occur, may be covered by a small deduction from the dividends for several consecutive years.

Charges to Capital.

Thirdly, as regards expenditure incurred in extensions of business. Such outlays of capital may be made in various forms. A railway company, for the sake of extending its traffic and receipts, may make a costly bridge over the Thames; or establish a terminal station and a hotel in the heart of London; or it may lay down new rails to meet an increase of traffic on its existing line; or it may make a branch-line, or an extension of its

main line, to open up a new source of traffic. In each and all of those cases the outlay ought not, and cannot, be included in the working-expenses. It forms no part of those expenses. It is not a charge in connection with the present receipts of the company, but an outlay for the purpose of profitably increasing those receipts. Hence such an expenditure is not chargeable to Revenue, but to Capital.

Here we must offer a word of explanation. To the general public, the terms "charging to capital," "closing the capital account," &c., are not, we apprehend, very intelligible. "Charging to capital" means simply to pay a larger dividend than is furnished by the profits of a particular year. It is an appropriation of a portion of the capital to the payment of dividends. The company, obviously, is not any richer from this process, but the persons who are shareholders at the time gain more than they would otherwise do. In truth the company, as a permanent body, is *pro tanto* poorer by the transaction (*i. e.*, there is less profit to divide in future years), but the temporary shareholders are richer. In short, "charging to capital" is substantially an appropriation of a part of the prospective receipts of the company. It is a paying of interest on a sum expended with a view to increase the receipts of the company, during the interval which must elapse before the works so undertaken are completed, and in anticipation of the additional receipts thereafter to be acquired.

For example, say that a company, for the sake of extending its traffic and receipts, makes an outlay of £100,000 upon works which cannot be completed until

the lapse of two years. Then, as this sum is "charged to capital"—in other words, as interest has to be paid on it to the shareholders for two years, although no additional receipts are acquired,—instead of raising simply the £100,000 needed for the works, nearly £110,000 must be raised, in order to pay the two years' interest at 5 per cent. This sum (whether subscribed by the shareholders or raised by debentures) becomes part of the permanent capital of the company. Then say that in the third year this outlay bears fruit in an increase of net receipts of £6000,—equal to 5½ per cent on the £110,000: in such a case the position of the company, even after paying interest on the sum for two ye ars a 5 per cent, is better than before. If the interest on this outlay were not "charged to capital," the shareholders during the two years when the works were simply in progress, and therefore yielding no return, would lose 5 per cent on this sum, solely in order that, after the expiry of the two years, other shareholders might gain 6 per cent; whereas by the system of charging such expenditure to capital, the present shareholders are adequately compensated for the investment, while the shareholders of the future are, it may be, still better off.

Of course, if such outlays are foolishly made, the system of charging to capital temporarily compensates the shareholders, while increasing the future loss of the company in connection with this investment. If this extension of the company's business when completed yields only 4 per cent, while the shareholders for two years have been paid 5 per cent on the amount, then of course the subsequent position of the company is slightly

impaired. But such investments are a mistake. The money for them would not be subscribed at all if they were not expected to pay 5 per cent. Hence the mere possibility of such outlays proving unremunerative cannot be advanced as a reason against the present system of charging to capital the interest on the amount while the works are in progress.

Again, an expenditure may be made not in the hope of acquiring new traffic or an addition to the gross revenue of the company, but for the purpose of lessening the annual working-expenses. In this case also, the interest on the sum expended may fairly be "charged to capital." It is a reproductive expenditure: for, though the gross receipts of the company remain as before, the net profits in future years will be increased.*

It has been frequently maintained of late, that every railway company should "close its capital account" after a certain number of years. This is a very erroneous statement. It is not a question of time, but of opportunity. To "close the capital account" simply means not to extend the business of the company. If there is no opportunity for profitably extending the business of a company, then the "capital account" may be closed at once. On the other hand, if there is a profitable field for extending its operations, the mere length of time that a company has been in existence in no way affects the question whether or not the company should undertake this extension of its business. It is simply, we repeat, a question of profits, of opportunity,—not of time.

* See Appendix.

A much more important question in connection with "capital accounts," or "charging to capital," has recently been discussed in a series of leading articles in the *Times*. In these articles it has been maintained that there should be no "charging to capital" at all, and that the dividend of a company should never exceed the net profits made by the company during the particular year. At first sight, it may seem a self-evident proposition that a yearly dividend should not in any case, or to any extent, be paid out of "capital," and should only be drawn from the actual revenue. Nevertheless, if the question be regarded from a practical point of view, it will be found that this proposition, so far from being an axiom, is absolutely erroneous. It will be found that the revenue of a railway company for any one year is no absolute criterion for the amount of dividend which such a company should pay. In some cases, the dividend paid ought to be *less* than the actual revenue of the year; in other circumstances, it may legitimately be greater.

As already shown, in the initial years of a railway the dividend ought to be less than the amount of revenue received; seeing that a portion of these profits ought to be set apart as a reserve-fund, in order to meet the heavy expense requisite in some future year or years in replacing alike the permanent-way and the rolling-stock. On the other hand, the dividend may legitimately be greater than is justified by the receipts of any particular year or years during which a company has made an outlay, a new investment of capital, for the purpose of extending its business and its profits.

We have already, by anticipation, touched this ques-

tion: but let us now consider it fully. Say again, that a railway company, for the sake of increasing its traffic and receipts, makes a costly bridge over the Thames; or establishes a terminus and a hotel in the heart of London; or makes a branch-line or "extension" of half-a-dozen miles, to open up a new source of traffic. In such cases, £100,000 may be expended in a single year without any return. Yet the position of the company may remain as good, or may be better, than if no such (temporarily profitless) expenditure had been incurred. Are the shareholders, then, to receive no dividend at all for that year, merely because the net receipts of that year only cover the expenditure, although the financial position of the company, the actual value of the railway, is at least as great as ever? Even private traders do not act on such a principle; they do not reduce themselves to starvation every time they invest their money in business: and still less is such a course applicable to the management of a public company. The principle is wrong in itself—it is erroneous in all cases; but it is especially inapplicable to railway companies. Consider the facts of the case:—

Requirement for Steady Dividends.

The expenditure and receipts of a railway company cannot be dealt with in the same fashion as those of an individual trader. The money invested in railways is a portion of the surplus wealth of the country,—a part of the reserve-wealth of many hundreds or thousands of individuals, who do not choose to trade in that wealth on their own account. A farmer who, fortified by a

long lease, employs his capital in reclaiming waste lands—or a manufacturer who enlarges his factory, or adopts new machinery of a better kind, or who builds a new factory for the enlargement of his business,—may possibly submit to the temporary decrease of his receipts, occasioned by this outlay, for the sake of the increased profits which he will make in future years. But the case is different, and must be different, with railway-shareholders. They are not permanent but temporary investors. The money which they invest in railway-shares is a temporary investment. It is their reserve-wealth: and what they especially require is, that they may at all times have the power to recover that wealth —to re-convert it into money. Every year the share-list of a railway company varies, some men selling out and others buying in. The prime value of railway-shares, in fact, consists in their value as reserve-wealth,—as a negotiable commodity convertible into money at will.

But this quality of railway-shares would entirely disappear if the dividends payable on them were to be regulated solely by the net receipts of each particular year. If a line which ordinarily pays 5 per cent were, in some year, to pay no dividend at all, the price of the shares would be immensely depreciated below their ordinary value, although the actual value of the line remained as good as ever; and for this reason, that the only index of the profitableness of a railway to the general public is the amount of its dividend. We repeat, the capital invested in railways is a portion of the surplus wealth of the community, and it is impossible to expect that the general public can ever enter fully

and minutely into the financial position of a railway company. If the general public is to continue to invest in railways, there must be some clear and definite proof that such investments yield a fair amount of profit.

A private trader knows his own business thoroughly. Whether it be a farmer who invests his spare wealth in reclaiming waste lands, or a manufacturer who extends his factory or replaces his old machinery by new and more profitable appliances,—in all such cases the individual trader knows exactly what he is about. But, we repeat, the persons who buy railway-shares belong to quite another category. They do *not* employ this portion of their wealth in their own business,—in many cases they are not traders at all; they simply make an investment in a kind of business which they think will yield a fair return, but of the details of which business they know little or nothing. If it were necessary for them to master all the questions of railway-management, they certainly would not invest their money in shares which yield only 4 or 5 per cent. Even a farmer, whose capital yields less than any other trader's, expects a profit of 8 per cent, and a manufacturer or shopkeeper expects double that amount. It is only because the investors in railways do not expect to be compelled to master all the details of the business,—it is only because they are entitled to regard themselves as "sleeping partners,"—that they are willing to invest their money in such undertakings at 4 or 5 per cent.

What follows? Simply this,—that there must be some patent means of showing the profits of railway companies, as an index to the general public who sup-

port such enterprises. And there is, and can be, no index of this kind so efficient as the rate of dividend which those companies pay. The shareholders, we repeat, are a fluctuating body, and the first requisite of railway-shares is that they should command a steady price in the market. Yet this is impossible if their dividends are liable to fluctuate from 5 per cent to *nil*.

Accordingly there are two important respects in which railway-property differs from that of a private trader. As the shareholders are a fluctuating body, it is imperative, as an act of simple justice, that the dividend should every year be equal to the current value of the property, as represented not only by the actual revenue, but by the interest on any outlay of capital invested for the purpose of increasing the receipts of future years. In the case of a fluctuating body of shareholders it is actual injustice to reduce the dividend of a particular year, when an outlay for new works is being made, simply with the result of greatly adding to the dividends in future years after the works are completed.

This is the main point. But, secondly, whether the dividend is to exceed the revenue of any particular year, by the payment of interest on capital which is temporarily unprofitable (*i.e.*, during the period when the new works are in progress); or whether the dividend is to be kept below the revenue, in order to form a reserve-fund for inevitable replacements of the property: in either case, a great object is attained,—namely, that of keeping the dividends at as steady an amount as is compatible with the circumstances of the railway, so

as to be a true and fair index of the company's financial condition.

Audit of the Accounts.

As has been shown, one important means towards placing the credit of railway companies on a sound footing, is the adoption of a uniform system of railway accounts, drawn up on the principles which we have enunciated. But another point is also requisite,—namely, that there should be a suitable guarantee for the genuineness of the accounts so rendered. How is this to be obtained?

For the Government to undertake an official audit of the accounts of railway companies is a course not likely to be adopted. It is open to several objections. To extend such an audit to the accounts of all the joint-stock companies of the kingdom is really impracticable; and to restrict it only to railway companies would be an expenditure of the public money which might justly be objected to by the community at large. Moreover, if this audit were made by the Board of Trade, the Government would be directly responsible for the correctness of all the accounts thus audited by its officials; and, if any serious errors occurred in the balance-sheets thus issued "by authority," the Government would, morally at least, be responsible for any loss to individuals arising from the misrepresentation of a company's financial position. If an individual, relying upon the Government balance-sheet of a company, were to invest largely in the shares of that company, and were thereafter to incur heavy loss upon the investment

in consequence of the audit having misrepresented the financial position of the company, it is difficult to see upon what ground the Government could resist a claim for compensation.

But the matter could be satisfactorily arranged in a slightly different form. The prime requisite is simply that the accounts should be made up on a uniform system, and that the audit should be made by competent men whose position shall be such as to free them from any motive for, or suspicion of, partiality. The auditors at present employed on railway-accounts are not so circumstanced. They are dependent for their salaries upon the companies whose accounts they are employed to report upon. The prime requisite of the case, then, is, to render the auditors of railway-accounts independent alike of the directors and of the shareholders. This object could be fully attained by the establishment of a Board of Railway Audit, the members of which should be appointed by the Government simply in its capacity as a neutral and competent party. The Government, of course, will be responsible for the appointment of competent men, but no further. And the expenses of this Board of Audit will be borne by the companies which desire to avail themselves of it. The duties of the auditors thus appointed will be to see (1), that the accounts of the railway companies are made up in accordance with a uniform system to be agreed upon; and (2) that these accounts are genuine. It might also be enacted that the directors be held penally responsible for *bona fides* in the statement which they render of the company's accounts.

But these auditors shall have no power to prescribe the amount of dividend to be paid by any company. The statement of accounts thus drawn up in the prescribed form, and duly examined by the Board of Audit, will be submitted to the shareholders; but the balance thus shown will not necessarily regulate the dividend to be paid by the company. That is a matter which must be left to the shareholders themselves. They must be left free, as at present, to make any dividend they choose. They may divide less than the total amount of the half-year's profits, if they please (devoting the surplus to the establishment of a reserve-fund, which would be a good innovation on the present practice),—and they are not likely to err in this direction. But they must also be left free, as at present, to make the dividend larger than is justified simply by the half-year's receipts,—seeing that frequently they have to make an outlay which, though essentially wise and profitable for the company, does not yield any return during the half-year in which it is made. A railway company is quite as much entitled to draw occasionally upon the profits of the future as a private trader is; nor is it possible for a fluctuating body of shareholders to carry on their business properly without this power.

Insolvent Railways.

A Railway differs in many respects from other kinds of property: accordingly the law relating to insolvent railway companies is of a peculiar and exceptional character. The rights of creditors have to be subordinated to the interests of the public. A creditor is not

allowed to impound any portion of a railway company's property; for such a seizure of the rolling-stock or other adjuncts of the line would stop or impede the traffic, and thereby seriously inconvenience the public. Nor is any creditor allowed, by promptitude in establishing his claim, to obtain priority of payment over the other creditors: whether he be a debenture-holder or a common creditor, he is only entitled, in the case of an insolvent company, to rank *pari passu* with the class of creditors to which he belongs. This is expedient for the interests of the public; but it is also a great advantage to railway companies: for it insures that the bankruptcy of a railway company will not be occasioned by the mere action of a sharp-witted individual, but will only take place when the company's embarrassments have become so serious as to induce a large body of the creditors to agree upon this course.

Another peculiar difference between an insolvent railway company and ordinary bankrupt concerns is, that a railway company cannot die. However burdened with debt, it remains immortal. When a private individual or an ordinary company fails, the business in most cases simply ceases; and the goods or buildings connected with it are sold off to different purchasers. But a railway, once made, remains an enduring fact: public interests require that it shall not be dismantled, destroyed; and in order to its working, there must always be a Company. Individual shareholders in an insolvent railway may sell out,—but the Company, as a corporate body, must continue to exist.

Doubtless the same object would be attained by allow-

ing one company to expire and another to take its place, —by the process of selling the bankrupt railway to purchasers, who would form themselves into a new company. And unquestionably this is the most natural course to take. It is only treating a bankrupt railway company on the same principle as other bankrupts. And this was the course originally proposed in the Bill brought forward last summer by the Board of Trade. But it was vehemently opposed by the railway companies: specially on the ground that a railway, if put up for sale, would not realise anything like its value, owing to the impossibility of securing effective competition,—the bidding, they said, would practically be confined to a few great capitalists, or to public companies, who would profit largely by their exclusive possession of the field. This would be true if a railway were put up for sale "in block." But such a mode of procedure is not necessary: the property might be put up in lots or shares, say of £100 each, to public competition,—with the proviso that no purchaser should be bound by his offer unless the whole property were sold. The purchasers of the railway would then constitute a new company, and the line would be worked as before.

The opposition of the companies, however, was successful: the clause providing for the sale of insolvent railways was struck out of the Bill: and in lieu of it the following plan was adopted and embodied in the Act. Any company which cannot meet its engagements may file in Chancery a "scheme of arrangement:" whereupon all actions against it will be suspended, and the company will be allowed at least three months to obtain the

assent of its creditors to the proposed arrangement. If this assent be obtained, the company, subject to this arrangement, will carry on its business as before. But if no "scheme of arrangement" is filed by the Directors, or accepted by the creditors and shareholders, then any creditor who has obtained a judgment against the company may, "by a petition in a summary way to the Court of Chancery, obtain the appointment of a Receiver, and, if necessary, of a Manager;" and the net revenue received by these officers shall be applied in payment of the debts of the company, "according to the rights and priorities" of the creditors. When all the debts are paid off, the duties of the Receiver and Manager will cease: and the company, released from Chancery, will then go on as before.

Under this plan, the security of railway creditors is not so good as if an insolvent railway were liable to be sold, like other bankrupt property. It is true that the whole net revenue of an insolvent railway is secured for the creditors; but this provision by no means insures a *prompt* settlement of the company's debts,—seeing that these (including the debentures) greatly exceed the annual revenue of any line. Whereas, if insolvent railways were put up to sale, the proceeds would suffice to pay every creditor promptly and in full.

Doubtless, this important change in the Bill was made chiefly out of deference to the exceptional difficulties of the time. A large number of railway companies are in an insolvent condition, and an absolute panic prevails in regard to railway property; and if the lines belonging to those companies had been put up for sale,

the result would have been disastrous beyond measure to the shareholders. We feel confident that such a state of affairs is only temporary, and that in future the bankruptcy of a railway company will be an exceedingly rare event. Nevertheless, the plan now adopted for dealing with insolvent railways is open to no very serious objections; and undoubtedly it is a great improvement upon the previous state of the law.

The only suggestion which we have to make relates to a matter of detail. The Court of Chancery has no special knowledge of railway affairs. If—as is usual—officials of the bankrupt railway be appointed to conduct the liquidation, good and well. But if it be found necessary to depart from this course, then we think that the duties of the Receivers and Managers should be discharged by members of the Board of Audit,—officials who would naturally be fully competent for such work. It is notorious that individuals occasionally seek to force railway (as well as other) companies into Chancery, in the hope that they may obtain lucrative appointments in connection with the insolvent property. Moreover, as the Receivers and Managers to be appointed by the Court of Chancery would receive salary according to the length of time they are engaged in the work of liquidation, they would have a motive for prolonging the work as long as possible. No suspicion, even, of such a motive could arise if the work of liquidation were discharged by the proposed Board of Railway Audit. The members of that Board would receive fixed salaries, and consequently would have no motive for prolonging their work.

Moreover, the more numerous such a Board can be made, with due regard to economy, the more efficient will it be. If such a Board were established, we believe every railway company in the kingdom would willingly avail itself of this neutral and authoritative audit of its accounts. And as the insolvency of a railway company will, we firmly believe, be a very rare occurrence in the future, we think that the liquidation in such a case might be efficiently discharged by this Board, without greatly adding to its labours; while the payments made for conducting such liquidations would enable the State to constitute the Board of Audit on a footing of most perfect efficiency.

THE FUTURE OF RAILWAYS.

Despite the present depressed condition of railway property, we believe that of all the numerous lines now constructed there is not one which is not fitted to become remunerative. We do not say that every one of them will yield an adequate return on the capital originally invested in it. That, in truth, is a question of the Past. The exorbitant portion of the capital invested in railways has now, practically, been struck off and put out of consideration, by the proportionate fall that has taken place in the value of the property. The discount on the shares of the mismanaged companies represents that amount of misspent capital. But, at present prices, we believe there is no railway in the kingdom which does not present a fair field for invest-

ment. Not merely the immense moral depression occasioned by the Panic and damaging revelations of the past year, but also the abnormal depression of Trade, have sufficed to reduce the price of railway-shares below their just level. And as the feeling of panic and distrust wears off, and the industrial energies of the country resume their normal progress, the value of the shares will unquestionably rise.

In fact, the future is full of solid hope. The construction of railways is far from being at an end. It must and will go on. And all of those *new* lines will be so many feeders to the lines already constructed. Nearly all the trunk-lines which the country requires are already made: so that the new lines will be almost exclusively branch-lines, bringing down traffic to the existing lines. It is as if all the great river-courses of the country were excavated, and partially filled with the superabundant waters, while their tributary rivulets had as yet hardly begun to flow,—had not yet established beds for themselves, and only reached the main rivers sparsely and defectively, trickling down the hillsides and percolating slowly through the marshy flats of the valleys.

The general belief at present, even among those who take the most hopeful view of the work of railway-extension, is, that all that remains to be accomplished in the future is the construction of branch-lines. And this, we have said, will certainly be the main form of railway-extension in the future. But urban and suburban railways will ere long be constructed in great numbers. And also, we believe, a new kind of rail-

ways—lines with a different purpose than any already in use — will, to some extent, come into play. We mean lines specially constructed for rapidity of passenger-traffic. At present, no mere passenger-lines will pay, — except purely city lines, like the London Metropolitan. But in course of time the case will alter. "Time is money." Every hour saved in transit from place to place is so much gain to the man of business. Hence we believe that ere long we may expect to see some lines constructed especially for rapidity of transit,— taking a straight course from starting-point to terminus, and devoted specially to express-trains for the conveyance of passengers.

But, putting aside these exceptional lines, which necessarily will be very few in number (and most of which will doubtless be constructed simply by widening the present trunk-lines, and devoting the new rails to express-trains), let us consider railway-extension in the main form which it will take: namely, the construction of branch-lines,—or rather, minor lines, connected with the great lines, but most of them worked by independent companies, and many of them constructed on a narrower gauge.

The superiority of steam-power to horse-labour is one of the elements of our industrial progress. This is more and more acknowledged every year in all forms of production; and steam will continue to displace, or at least more and more supplement, horse-power as a means of locomotion. Every town at present unconnected with our railway-system will ere long place itself in connection with those great

arteries of traffic by a branch-line of its own. And every valley or rural district where horse-power alone is at present used as a means of locomotion, will soon supply itself with means of transit in the superior form of a railway.

Railways, in truth, have already far overpassed the limits originally assigned to their power. They now can ascend heights which were formerly deemed insurmountable by them; they also can wind round curves, and a succession of curves, of almost as small a radius as that which is thought safe for horse-traffic. But more than this is wanted in order to carry the advantage of the railway-system into our agricultural valleys and outlying districts. That those valleys, however steep and winding, can be penetrated by railways, we do not consider doubtful. But then, there must not only be the power of railways to do this: there is the other indispensable requisite that the work should be done *cheaply*, so that those sparsely-peopled outlying districts may be able to avail themselves of this superior mode of locomotion. In such purely rural railways—mere feeders of the rapid trunk-lines—speed is not wanted. A rate of ten or twelve miles an hour is ample. Now this low rate of speed will at once supply the element of cheapness. At such an average speed, curves as sharp as any that are needed may be safely encountered; the line may wind as much as any ordinary hill-road. The gradients may also be of the steepest. And lastly, the rails may be very light compared to those on our present lines, which are made for a ceaseless traffic at a high speed. Low speed, light rails, and

a narrow gauge,—these are the only requisites for a profitable extension of the railway-system to our agricultural districts. And the advantages of the introduction of railways into those outlying districts would be immense. It would not only diminish the cost of conveying to market, sheep, cattle, and the produce of the fields; but it would enable farmers to get upon easy terms a supply of lime, manure, and all the other requisites of production: so that the producing power of our outlying agricultural districts would be vastly increased. The reclamation of waste lands, and the improvement of lands already under culture, would thereafter go on with a rapidity impossible before.

Next, let us consider the financial method to be employed in the construction of these new lines. Firstly, as regards the few lines specially adapted for rapidity of passenger-traffic. These will necessarily be constructed by the same method as that which now prevails,—namely, by companies whose shareholders are drawn from the general mass of capitalists in the kingdom—from men whose only motive for subscribing is a desire to get a good profit on the money which they invest in the undertaking. Secondly, in regard to the branch-lines, either (1) connecting towns at present isolated from our railway-system, or (2) opening up outlying rural districts. In both of these cases the enterprise will be purely local —undertaken solely by the inhabitants of the district.

Let us take the second of these cases first. It is obvious that the persons who will chiefly and most permanently gain by the construction of such rural lines are the Landowners. For the sake of permanently increasing

the value of their land, these men will be the chief promoters of the new lines. They will be the largest subscribers, and will also give the ground for the railway either gratis or at a merely nominal price. The Farmers will also take shares in the lines, especially when they hold leases; and it is not improbable that the landowners, for their own interest, will specially extend the leases of those tenants who are willing to become subscribers to the undertaking. In this way—the enterprise being purely local—there will be no rivalry between the interests of the railway company and the interests of the local public. The men who need the railway will also be its shareholders. So that the running of the trains, and the charges for traffic and transit, will be regulated in exact conformity with the interests of the local public. In fact, it will be the excellent system of Co-operative Societies applied to the construction of railways.

2. If the motive for the construction of a branch-line be not so much the opening up of an agricultural district as the interests of a little town which desires to place itself in connection with the railway-system of the country—and generally both of those motives will coexist,—it is obvious that the Town itself, as a corporate body, will have to undertake a part of the subscriptions to the new line, in addition to the Landowners and Farmers whose property will be benefited by the undertaking. This brings us to another new feature in the work of railway-extension. For we believe that ere long, Parliament, in answer to the desires of the community, will pass an Act for the special purpose of enabling townships or districts to levy a rate for the

construction of railways, — just as at present for the construction and maintenance of roads. In course of time there will be Railway-rates, just as there are at present Highway-rates.

But, it may be asked, what, in such an eventuality, is to become of the highroads thus supplanted by railways? In many districts, we believe, the existing roads will be converted into railways. Or a part of the road will be appropriated to the railway, leaving the other part for horse-traffic and foot-passengers. Moreover, we believe that in a few years hence the appliances of steam-traction will be modified so as to permit of a locomotive running upon ordinary roads. It is merely a question as to the construction of the wheels: the object to be attained being simply to give the wheels a sufficient hold on the surface, without producing an excessive wear of the roads.

In fine, Railways in the future will in all localities become as necessary as highroads are at present: and our legislation will have to bring itself into accordance with the altered circumstances of the time. Instead of public companies as at present, local companies will come into existence with the railway-extensions of the future. And also, local communities will seek and obtain legislative authority for borrowing money for the construction of railways, just as they do at present for the making of roads.

XXVIII.

MUNICIPAL FINANCE

We are at the outset of a new era in social progress, and one which is probably the highest to which material civilisation can attain. It is the era of Co-operation. Hitherto Competition has been regarded as the most efficient agent of social progress. But the principle of competition is one of rivalry and struggle—it is a system of beggar-my-neighbour—most useful in the earlier stages of civilisation, but one most unworthy of civilisation in its maturity. It is costly, for it requires many companies and establishments to do the work which would be more economically performed by one; and it is full of social unhappiness, and fruitful in the bitter feelings of rivalry and jealousy, because each establishment seeks its gains at the expense of the others. The new system of Co-operation, on the other hand, seeks to unite and fuse into one the hitherto rival interests of the trader and his customers, of the consumer and the producer.

By-and-by the system will be more fully developed, and the social advantages will be commensurately increased. Say that a little town is desirous to supply itself with gas or water; then a company will be formed, with a capital apportioned in many small shares, so that almost every householder may be a member. In this way the company will insure for itself the largest possible number of customers: opposition and jealousy will disappear, and the little community will have but one interest in the matter. In like manner, a town may supply itself with bread, or groceries, or butcher-meat, or any other article for which there is a general demand. The employés, too, of the company, by holding shares in it, may be made to participate in its interests, and to discharge their duties with more scrupulous diligence than is usually to be found in a hireling or salaried agent. No doubt the time is still distant when the system of co-operation shall reach this development; nevertheless, its coming may be calculated upon. And thus, at the present hour, we are witnessing the initial stage of a principle which will revolutionise our system of industry, and accomplish results fraught with a vast increase of happiness and prosperity to the community.*

So we wrote four years ago. Since then, the Co-operative principle has been steadily rising into wider notice and greater favour. The advantage of the principle is now fully acknowledged; and there can be no doubt that every year will see its application more extensively developed. The object of the present chapter

* See the *Economy of Capital*, p. 155-57.

is to point out how advantageously, and on what a large scale, this co-operative principle may be applied in the case of cities, towns, and suchlike corporate bodies. In little towns the system may be more fully adopted than in the case of large ones: it may be applied to the supply of various articles of general use,—the supply of which, in large cities, must in the main be left to private enterprise.

But there are at least two important matters in which the principle can be adopted with immense advantage by all municipal bodies—by all towns, whether large or small. These two matters are the supply of Gas and the supply of Water. The supply of these commodities is a business which every township or municipality should, and can advantageously, take into its own hands. It is a kind of business more suitable than any other for the management of a municipality. As soon as the primary works are completed, the duties of management would be easy and simple. Any kind of business which requires a daily superintendence—where the conditions of the business fluctuate from day to day, or even from week to week—is not very suitable to public bodies, and ought generally to be left to private management,—both on account of the close attention which such business requires, and also owing to the *risks* which attend it. But the case is different with the supply of gas and water,—where there are no fluctuations, and where the only change which takes place is a gradual increase in the demand for the commodity supplied.

The supply of water and of gas must always, practi-

cally, be a Monopoly: and a Monopoly, in the hands of private parties or companies, is, as regards the public, a most disadvantageous form in which those indispensable requirements of life can be supplied. In such a case, the public is at the mercy of the monopolists. The public cannot do without gas and water,—they must remain customers of the companies, — neither, practically, is there any means of bringing into play the ordinary principle of Competition. Moreover, where, as in large cities, there are more companies than one, serious inconvenience as well as expense is occasioned by the breaking up of the streets by these companies, and the laying of two or more lines of pipes where one would suffice. On the other hand, if the Municipality takes the business into its own hands, those evils are fully remedied, while, in all probability, an actual gain will accrue from the undertaking: thereby lessening the burden of local taxation, or creating a surplus which can be devoted to important civic improvements.

The advantages of such a system would be twofold—alike economical and social. There would (1) be not only the acquisition by the public of the prospective profits on the supply of gas and water, but also an immediate advantage by the more economical management of the business; and (2) there would be a greater satisfaction on the part of the public, seeing that they would no longer have to deal with private companies, inclined to extortion, but would actually have the management in their own hands. Instead of the existing conflict between the interests of the Public and of the Traders, we should have a Co-operative System under

which this antagonism of interests would disappear. There would be no motive to overcharge, and the commodities would be supplied at prime cost. The community, in fact, would be alike the producers and the consumers.

In the case of towns which have not yet obtained a supply of gas, or a regular service of water, the system of municipal action which we advocate can easily be adopted. But, as needs not be said, there is hardly a town of any size which is not now supplied with gas and water by private companies. Hence, while advocating an opposite system, not the least important and certainly the most difficult point is, to show in what way the new system can be applied under existing circumstances; and especially in what way it can be adopted with a due regard to the vested interests of the private companies. A wise and just arrangement of the kind must effect a reconcilement of the rival interests of the Public and of the Companies, by a financial process perfectly fair and permanently advantageous for both parties. A great benefit for the public, for the inhabitants of each township or city, must be attained without unjustly affecting the rights of the existing companies.

The only manner in which such a system of Municipal finance can be adequately explained and developed is by taking a typical case, and showing in detail the mode of procedure and the various considerations which have to be taken into account. For this purpose, alike as regards the magnitude of the operations, and the variety of points to be dealt with, the case of London is

of all the others the best. Accordingly we have treated the case of London, in its relation to Municipal finance, in full detail in the Appendix:* which appears to us a better place for such an exposition than here,—seeing that such a statement of a particular case would too much interrupt the general progress of this work.

* See Appendix,—"The Gas and Water Supply of London."

XXIX.

LAND FINANCE

It has been a matter of general surprise, on the part of historical writers, that the Founder of the Bank of England (William Paterson) should have so soon resigned, or been ejected from, his post as one of the Directors of that establishment. There has been much conjecture as to the cause of his withdrawal. One of the most prevalent conjectures attributes his fall to the fact that he was a Scotchman,—the prejudice against Scotchmen at that time being so strong in England that it amounted to actual antipathy. It was English jealousy, given effect to by William III., that mainly ruined the Darien scheme; and unquestionably Scotchmen were at that time in very bad odour in England and at Court, —Scotland being the stronghold of the supporters of the exiled Stuart dynasty. The other conjecture is, that Paterson was too much a man of theory, and lacked the practical business-talent requisite for the functions of a Bank Director. For this conjecture there is certainly no

ground. It is opposed by the well-known character of the man. Paterson was practically conversant with commercial business, and also proved himself an eminently safe as well as able adviser in all questions of finance. He possessed talents and energy of the highest order: and, apart from the originality of his genius, it may safely be affirmed, that if he has ever found his equal as an able and safe financier among subsequent Directors of the Bank of England, he has never found a superior.

A rare pamphlet, preserved in the Library of the Board of Trade, has recently come to light, which dispels both of the above conjectures, and shows clearly the cause of Paterson's withdrawal, or ejection, from his post as one of the Directors of the Bank of which he was the founder. From this pamphlet it appears that, after organising the Bank of England as an agency for applying the credit-system alike to State-finance and to the general trade of the country, Paterson proposed to organise a sister-establishment, a Land Bank, for applying the credit-system to the soil and its products. This proposal at once aroused the jealousy of his fellow-Directors. It seemed to them that if such an establishment were created, it would trench upon their own ground and diminish the profits of the Bank of England. Hence they not only opposed the project, but made Paterson's position at the Board so uncomfortable that he felt compelled to resign.

In this project for the establishment of a Land-Bank, as in many others, Paterson was in advance of his age. John Law, indeed, afterwards took it up, with that hazardous brilliance which Paterson constantly opposed in

finance: and, as is well known, the scheme failed,—though not solely, or even chiefly, from the fault of Law's plan itself. The project was never entirely forgotten. For example, in the early years of our American colonies, land-credit, in a rude form, constituted one of the chief adjuvants of the wonderful progress then made in reclaiming the wilderness of nature. But it is only recently that the idea of organising financial establishments for the special purpose of applying the credit-system to land has again been taken up. Although it was in this country that the project was first proposed and planned, it is on the Continent that it now finds most support. The Credit Foncier has rendered vast service to the small landholders of France. And to a Belgian, M. Langrand Dumonceau, belongs the honour of developing, on a grand scale, an organisation of Credit as applied alike to Land and to Agriculture. He found land-banks and land-bonds already in existence in Germany; but he has widely extended the benefits of such institutions, and he has also introduced most important improvements in their organisation and practical working. Whether he will reap an adequate reward for his labours, is still doubtful,—the recent and still prevalent financial depression having necessarily greatly obstructed his operations. But whether he succeed or not as a question of personal gain, there can be no doubt that his labours will not be lost; for his scheme is fitted to confer a benefit upon the world at large, and will be carried out by others, even should he himself be unable to work it solidly and successfully.

Credit is the great lever of Production: and it is cer-

tainly a remarkable fact that the Land, the most solid and permanent of all kinds of property, should be the last to be brought within the sphere of its beneficent operations. As regards Commerce and Manufacturing industry of all kinds, the invaluable aid of the Credit-system has been applied to them with an elaboration which is a marvel of civilisation, and with a completeness that leaves nothing to be desired. The Land, on the other hand, has hitherto been treated as a Pariah. It has been comparatively excluded from the benefits of the Credit-system. It has been neglected: no one has thought of creating for it financial establishments like those which have conferred such inestimable aid and benefit upon commercial and manufacturing industry.

Why is this? At first sight it seems astonishing that the most solid and stable of all kinds of property should have been virtually excluded from the operations of the Credit-system, while the more perishable and less solid and less locally fixed products of trade and manufacture should have been so thoroughly brought within the operations of financial economy. But there is a great point of difference. There are two special hindrances to an extension or full development of the Credit-system as applied to Land and Agricultural property. One of these pertains to the nature of the Land itself; the other to the present laws in regard to Land and its products. The latter point—embracing the operation of the laws of Entail and of Hypothec—is too wide to be here discussed. We shall confine our remarks to the other point:—

(1) Land, although the most stable of all kinds of

property, is the *least negotiable*. It cannot be sold—*i.e.*, converted into money—with the same ease and promptitude as merchandise. A consignment of merchandise can be sold piecemeal,—so many tons of iron or bales of cotton to one man, so many to another; and each of those commodities possesses the same value in parts as if sold in mass. But it is otherwise with Land. In the first place, the cost of selling, or transferring the possession of, land is much heavier than is the cost of selling goods; moreover, this cost does not diminish in proportion to the value of the land sold. The sale of a small property is proportionately more costly than the sale of a large estate. Secondly, Land practically cannot be broken up and sold in parts of very small value, as a consignment of goods can. Thirdly, chiefly from this cause, the demand for land is less steady and extensive than the demand for goods: that is to say, it requires men of capital to buy land,—and the number of capitalists is comparatively small. For these three reasons Land is less negotiable than most other kinds of property.

(2) Owing to the character of Landed property, loans upon land are always for much longer periods than loans upon merchandise. Merchandise is only produced, or purchased wholesale, for the sake of being immediately sold. It is meant to be converted into money immediately. A merchant who purchases a certain quantity of goods requires credit only for a short time,—only for three or four months. He gives his bill for that term (that is to say, gets credit), and before the term has expired he has re-sold the goods; and with the proceeds of the sale, he pays off the bill, and at the same time

pockets the profit on the transaction. Loans on land, on the other hand, must be for long periods. The soil yields its produce only annually: a year is the shortest time within which money invested in land is recoverable. And in most cases the loan must be for a much longer period. For example, if a landowner or a tenant-farmer gets a loan for the purpose of erecting farm-buildings, for draining the land, or even for liming or manuring a farm, the money so invested does not yield an adequate return for many years. Even a thorough liming of a farm does not yield its full return until after ten or fifteen years. The length of such loans renders them (speaking roundly) unsuitable to be made by banks: for it is the first requirement of safe banking that its loans should be for very short periods,—otherwise the capital of the bank is "locked up," and, in the event of a monetary crisis occurring, the position of the bank is thereby seriously endangered.

Thus, owing to its special character, Land is not so readily convertible into money as merchandise is,—which circumstance, *quoad hoc*, renders Land a less suitable security for loans. And secondly, the loans required in connection with land must be for long periods,—so that banks cannot safely make such loans to any great extent. Hence it is that land at present participates only to a comparatively small extent in the benefits of the credit-system.

Despite these hindrances to the development of Land and Agricultural Credit, the excellent working of our financial system has not left land and agriculture without important aid. As regards landowners, the system

of borrowing by mortgages is in general use: these loans being usually obtained from Insurance Companies, which can afford to lock up the greater portion of their capital for long periods, whereas banks can do so only very sparingly. Again, as regards the farmers, our admirably ramified banking-system has been of immense use. In Scotland, especially, where the system of "cash-credits" has been established for generations, and where every village has its branch-bank, the agriculturists have profited largely by the credit afforded by banks. In truth, in Scotland, by means of those branch-banks (the managers of which make it their business to be acquainted with the character and circumstances of the farmers of the district, and to make advances to them), the credit-system has been very fully applied to agriculture; and a similar state of matters is being developed in England. Moreover, Land-improvement companies have recently been established, which are calculated to render important service to the extension of Land and Agricultural credit. Nevertheless much remains to be accomplished: and we think it desirable, in this chapter, to consider the main points connected with finance in its relation to Land and Agriculture.

As regards the present system of land-credit—namely, in the form of mortgages,—there are the following drawbacks:—First, as regards the borrower. He is not in direct contact with the great mass of loanable wealth in the country,—which, speaking roundly, is represented by the deposits in banks. Unlike commercial bills, mortgages are not a kind of security in which banks deal freely,—partly owing to the long period over which

loans on land must necessarily extend, and partly owing to the difficulty of enforcing repayment of the loan. In consequence, banks will make advances upon mortgages only to the extent of two-thirds or three-fourths of the amount, whereas they will lend to the full amount upon a commercial bill. So that the effect is the same as if a landowner had to pay 25 or 30 per cent more for his loans than a merchant requires to do. Again, a landowner experiences a greater difficulty in finding a lender on his property than a commercial man does: he has frequently to employ an intermediate (usually his attorney) in such a matter,—whereas a commercial man goes direct to his bank. And, finally, a mortgage is far less easily extinguished than a debt contracted by the short-dated bills of the commercial classes. A mortgage is for a large sum, payable at the end of so many years, during which time the landowner has annually to lay by a certain sum in order to pay off the mortgage when it becomes due. It requires a great amount of self-control to do this: and, also, the money as it accumulates is likely (*quoad* the landowner himself) to lie unproductive in the interval.

Secondly, as regards the lender. The great drawback in this case is the difficulty of ascertaining whether the borrower's title-deeds are valid, and also whether the estate is not burdened by previous mortgages. And this difficulty necessitates the employment of an intermediate (usually an attorney), to make the proper inquiries. Thus, alike as regards the lender and the borrower, a loan upon land is a cumbrous and costly affair, compared with loans upon commercial securities.

The first and most easily adopted improvement in land-credit is, that mortgages should be made extinguishable not by one payment at the expiry of the time for which the loan is taken,—but by annual payments, embracing, besides the interest, a certain portion of the capital sum. This would greatly facilitate the extinction of mortgages: burdens which, under the present system, tend to become permanent,—the borrowing landowner in most cases being only too glad to be allowed to prolong the loan indefinitely, by merely paying the stipulated amount of interest: in which case he is really at the mercy of the lender, and is liable to have his property sold off to meet the mortgage,—the usual result being that he has to sell a part of his estate in order to clear off what ought to be, and was meant to be, a mere temporary loan.

Moreover, what is the position of the lender? Loans upon land are always and necessarily for long periods: and should the lender happen to want his money back during the period, he cannot (of course) get it from the landowner to whom he has lent it; at the same time, his mortgage-bond being a security not easily negotiable, he cannot get a loan upon it for anything like its full value, as he could do if he held a commercial bill.

Now, if loans on land were to be repayable (capital and interest) by annual instalments extending over the period for which the loan is made, this system would obviously be more convenient for the landowner than the present one; and also it would lessen the lock-up of capital on the part of the lender.

The next great desideratum is to bring the land-

owner who desires to borrow, into direct contact with the mass of loanable wealth in the country.

This can only be done by the creation of financial institutions which shall do for Land what banks do for Trade. Consider what is the real relation in which banks stand to trade, and what is the practical service which they render to the community. Banks deal in short advances: they issue banking currency (notes and cheques) in exchange for commercial currency (*i.e.*, bills), and also in loans upon the deposit with the bank of property of various kinds,—the borrower's whole estate also being liable in repayment. And the currency thus issued circulates freely: (1) from the fact that, in addition to the property in exchange for which the issue is made, the capital and credit of the bank are an adequate guarantee for the value of its notes; (2) that these bank-notes are payable in coin of the realm on demand; and (3) that they are for small as well as large sums, so as to be useful for all purposes. The *rationale* of the process is the same as if a bank were to take a bill based upon goods and guaranteed by two or more good names,—were to endorse that bill, thereby adding the credit of a great financial establishment to the commercial guarantee which the bill already possesses,—and were then to break up the bill into a number of smaller bills, for the convenience of the public, at the same time engaging to pay those bills (its notes) in coin of the realm whenever the holders of them should desire it. The merchants remain liable to the bank for payment of the bills; and the bank makes itself liable to the public for

payment of the notes which it issues in exchange for the bills.

The problem, therefore, is how to extend this credit-system, this process of financial economy, to Land on the same principle as it at present exists in relation to Trade. The main point to be achieved is to impart to mortgage-bonds a negotiability equal or approaching to that of commercial bills,—so as to render them fitting securities to be dealt-in by banks, and thereby bring borrowers upon Land into relationship with the mass of loanable wealth in the country. In order to accomplish this, there must be a class of financial establishments, intermediate between landowners and the banks, which shall impart to mortgage-bonds an increased negotiability so as to render them acceptable as securities by the banks and also by the general public.

Say that a Land-Credit Company is established, which invests its capital in loans upon land,—taking from the borrowing landowner a bond over the particular estate so mortgaged, and for payment of which he is also liable to the full extent of his means. This would be a process similar in kind to that by which a bank discounts, or lends its money upon, a commercial bill. The points of difference would be that Land is a much more solid security than merchandise, but on the other hand it is less readily saleable. Having received this security in return for its loans, the Company would thereupon issue bonds of its own, to the amount of its mortgages, but in smaller sums and for shorter periods. Say that such a Company lent £12,000 to a landowner for ten years—repayable, both principal and interest, by annual instal-

ments; it would thereupon issue bonds of its own to the same amount, but for sums of £50 or £100, repayable in (say) two or three years. These bonds would be greatly preferable to the original mortgage-bond, inasmuch as (1) they would possess an additional security in the guarantee of the Company; (2) because they would be repayable in a shorter time; and (3) because they would be for much smaller sums. Hence, these bonds would be far more negotiable than simple mortgage-bonds: so that ten or twenty individuals would be willing to invest their money in such securities for one that is ready to invest in simple mortgages. The bonds of the Company would be acceptable securities alike to banks and to hundreds of private individuals. And by this process the wealth available for loans on land would be increased ten or twenty fold.

Next, as regards the profits of such Land-Credit Companies. The rate of interest at which they made their loans to landowners would of course vary with the circumstances of the time. Say that they lent in ordinary times at 5 per cent: then they would issue bonds for the same amount bearing a somewhat lower rate of interest. And the difference between the rate at which they lent their money on mortgages and the lesser rate which they paid on their own bonds, would constitute the first profit on their transactions,—just as it does with the Land-Improvement Companies already in existence. But their profit would not end here. Their own bonds being taken up by the public, the money which they had lent upon mortgages would be returned to them: and a portion of that amount they

could invest in new mortgages,—again issuing bonds of their own for the amount. And the security for this second issue of bonds would, if the Company were properly managed, be as good as for the bonds first issued. In every case, at least, full value for the bonds would always exist in the shape of the land mortgaged, *plus* the personal security of the borrowing landowners: and there would be no more likelihood of the Company's "over-trading"—*i. e.*, incurring engagements greater than its reserve, or guarantee-fund, enables it to meet—than there is in the case of banks. In truth, as Land is of all kinds of property the most stable in value, there is less room for miscalculation in this kind of financial business than in any other. In fact (speaking roundly) the only fluctuation in the value of Land is on the side of increase. Land, in this country, steadily rises in value: whereas the merchandise, railway-shares, and other kinds of property upon which banks and discount-houses advance their money, are liable to very great fluctuations, on the side of depreciation, which in many cases it is impossible to foresee.

Such an extension of the credit-system would be advantageous not only to the Land but also to the general public: inasmuch as it would increase the forms of safe investment available to individuals, as well as to banks and insurance companies. But the prime benefit would be to Land, by extending to it the appliances of the credit-system, from which at present it is comparatively excluded.

It may be true that there is no urgent requirement for the establishment of Land-Credit Companies, such

as we have described, in this country: seeing that the object of such establishments is already in great part attained, either indirectly—that is to say, by means of insurance and other companies, which find it profitable to lend a portion of their money on Land,—or directly, by means of a few small establishments, like the Drainage and Land-Improvement Companies, which devote themselves to the development of particular branches of Land-Credit. But it is not less true that the system which we propose would be an improvement, an advance upon the present system. For example, loans were in use for thousands of years before Banking was introduced; yet no one doubts that Banking gives facilities for borrowing, and for the development of industry and wealth, totally unattainable before. In like manner, a good system of Land-Finance, by the establishment of great Companies whose special business is to make loans upon Land, will greatly aid the development of Land and Agricultural Credit, and thereby facilitate production in the most stable of all forms of national wealth. It is likewise true that the establishment of such Companies is in perfect accord with the spirit of the age,—with the progress of Finance, the development of the credit-system, which is indispensable in a progressive community, and to the maturing of the fruits of Civilisation.*

Although the main purpose of this book is to explain and to suggest improvements in the Financial system of this country, we are not without hope that the work may have a still wider application. And we are confi-

* See Chapters VI. and VII. of this work.

dent that the suggestions made in this chapter are fitted to be of much use in England's colonies, as well as in other countries where the Credit-system has as yet hardly been applied in any form to landed property, and to the development of the productive powers of the soil.

XXX.

THE STATE, THE POOR, AND THE COUNTRY

THE object of a Government is to do for a community what the community cannot do for itself. A Government consists of a body of men whose business it is to act as guardians of the general interests, and as administrators of the public affairs, of the nation,—*plus* a vast amount of wealth yearly placed at its disposal for the purpose of carrying out these objects. In a self-governing country like ours, the State is simply the Nation acting through a chosen body of administrators, —a Body to whom the Nation delegates its power for administering the public affairs of the commonwealth. Throughout this work we have earnestly discountenanced all unnecessary interference of the State in affairs of private industry and enterprise,—because such affairs do not come within its province, nor is the State well fitted for their administration. We hold that the State should engage in no business nor undertake any duty which can be equally, or even approximately, well

done by the public. This is a principle applicable to all Governments, but specially applicable in a country like ours,—which is thoroughly self-governing; and also where the governing body is liable to so many changes that it is impossible to carry out any scheme of policy extending over many years with the facility that is afforded for such operations under an autocratic or despotic form of Government.

In all the cases in which we have had hitherto to consider proposals for State-intervention, the only principle involved has been the simple question of finance. And in such cases, certainly in all of those with which we have had to deal, we think we have proved that no advantage is obtainable by such interference, even as a gain to the State. Nevertheless there are many cases in which the intervention of the State is not only justifiable, but urgently needed, for the sake of the moral and social wellbeing of the commonwealth.

The weak point of Political Economy has hitherto been that, by many of its teachers, the financial test has in all cases been made absolute. The immediate production of wealth has frequently been made the sole object of the science: overlooking the fact, not only that the amount of wealth in a community is far from being an absolute test of national wellbeing, but also that many an expenditure upon the improvement of the moral and intellectual condition of the people, howsoever unproductive in the first instance, or it may be for many years, transmutes itself into a positive financial gain in the end,—besides from the first conducing to the increased contentment and good order of the community.

In this, our concluding chapter, we desire to deal with some questions of this kind, as well as with others relating to the development of certain resources of the country which can hardly, if at all, be utilised without the intervention of the State.

The intervention of the State on behalf of the Poor, and of those weaker classes who are less able than the others to look after their own interests, is a natural function of all Governments, and is a recognised principle of the Government of this country. The poorer classes of this country have certainly not been neglected, either by the Government, or by the rest of the community. No Government can fix the rate of wages: yet even in this respect the condition of our working-classes is far ahead of that of any others in Europe. And if it be inferior to that which prevails in America, there are many advantages open to the poor and to the working-classes of this country, which are not possessed by the same classes in the United States. *There*, owing to special circumstances which no mere legislative acts can produce, the rate of wages is very high: but, except in regard to education, the Government declines to aid any one,—while the resources of private beneficence are infinitely inferior to those available in this country. With us, an immense sum is yearly raised in the form of Poor-rates, for the relief of indigence of all kinds. Hospitals, some of them possessed of princely endowments, exist in every city for the relief of the sick and the injured. Indeed, in this country, every ill that flesh is heir to finds an hospital, supported by private contributions, for its

special treatment. Age likewise has its asylums, where the aged and indigent find a comfortable shelter for their declining years.

Yet much remains to be done on behalf of the weaker classes in which the State must take a foremost part. The poor are a misery to themselves, and a burden and a danger to the community. Any prosperity which rests upon a vast substratum of pauperism is unsatisfactory and unstable. Unsatisfactory, because it is a slur upon Civilisation, and a source of unhappiness even to the wealthy, when alongside of great prosperity and wealth there exists a great amount of indigence and misfortune. It poisons the happiness of the prosperous, and forms a financial burden on the community. How can men be permanently happy when every day they see masses of suffering? One hot day last summer, a carriage drove up to Gunter's, in order that the fair occupants might enjoy his world-renowned ices: but a poor family stood, mother and children, at the door, begging piteously for alms: and the sight sufficed to spoil the intended indulgence. "How can we take this indulgence while these are starving?" and the ladies drove off. More or less, the same thing occurs to all of us. As we go along the streets, wrapped in warm coats, and with full stomachs, do we not every day, in this cold Christmas weather, come face to face with the poor crossing-sweepers and the piteous mendicants whom we so sedulously avoid: and does it not sadden us, amid our comfort, to see these miserable creatures?

The poor are a burden and a danger. Poverty breeds crime, as well as exacts rates. The more Poverty, the

more thefts and robbery, the more poor-rates, the more discontentment with Society and with Government. Poverty creates a hostile body, which wars against the rest of the community. Every family lifted out of indigence makes the political fabric stronger, the social body happier, the national wealth greater. One great end of legislation, therefore, should be to enable the working-classes to become less dependent for their daily food on their daily wages; and also to add to the producing classes the poor who at present cannot obtain work. If it were possible to take the idle population exactly to where they are wanted, the ranks of pauperism would be greatly thinned. We cannot do this by legislation alone. But are there not more means of employing this pauper class than have hitherto been called into play? We shall consider this question in the sequel: but first let us take the case of the Working-classes—the industrious portion of our lower orders,—and consider what means are available to help them to better their position.

First, as regards Education. The State makes every year a considerable expenditure for this purpose, in addition to the vastly larger expenditure from local and private funds. And although our educational system is still very deficient, the defects are so fully acknowledged, and the public is so ready to do its part in remedying them, that hardly another year will elapse before the system will be made as nearly perfect as can be hoped for. Moreover, if our primary education be very defective—if the means of educating the poor require to be greatly supplemented,—there is no other coun-

try of equal magnitude in which all the higher means of education and of intellectual culture are so abundant. Literary and educational institutions of all kinds abound —from simple reading-rooms and libraries, to others in which those accessories of culture are combined with educational classes, and with the delivery of lectures by men of high standing. Nor must we forget the important influence of the Press,—of the newspapers and cheap periodicals which flood the country with information and instruction.* Art-academies, also, are open to our artisans, raising their taste and increasing their industrial skill. We are far from holding that the means of Scientific and Art culture open to our working-classes are yet as perfect as is required, alike in the interests of our artisans, and for the sake of maintaining our superiority over other countries in the manufacturing arts. The more abundant those means of culture, the higher will become the character of our artisans, and the greater will be the productive power of the country. Our territory, our area of production, is unalterably fixed by the engirdling seas, but the development of the productive skill of our population is illimitable. If we are to maintain our present position—if Britain is not to decline greatly in the scale of

* "When I hear that the British people are not educated, that they are incapable of exercising what is very natural to a Briton, whether he possessed it before or not—namely, the exercise of the suffrage,—we forget that in this country there is a source of education perpetually going on, secular education of the highest class, which affords a future mine for the performance of public and political duties; and that is the influence, thank God! of a free press. That is an educational power of the highest influence."—*Mr Disraeli at Edinburgh; Oct.* 1867.

nations,—we must make up for the smallness of our territory by developing to the utmost the intelligence, moral condition, and productive power of our people.

The limitation by the State of the nature and hours of labour for women and children is another means of raising the condition of the weaker classes which is being earnestly applied by our Government. When the Factory Acts were first proposed, a great opposition was made to them, founded upon so-called principles of Political Economy; and a like outcry and complaint are heard in many quarters at present, in regard to the Act for extending the operation of those measures. It was at first, and is again now, maintained that the limitation of the nature of the work, and of the hours of labour, imposed by those Acts in regard to women and children, is calculated to diminish the productive power of the country. And so it is, in the first instance. But such Political Economy is not only heartless, but eminently shortsighted. It disregards two grand elements of the question,—the element of the Future, and also the question of social wellbeing. One object of those Acts is, to prevent the entire withdrawal of the Mother from the Home,—to secure for the children, the infants, of our poorer classes at least some portion of maternal care and training. The other object is, to prevent the over-working of children,—to prevent selfish and greedy parents from prematurely converting their offspring into a means of increasing their gains, at the sacrifice alike of the health and of the future moral and intellectual condition of those children. It is the duty of the State to take what means it can in order to

insure a healthy and educated people. Hence it is right for the State to step in, in the period of childhood, to secure so far as it can the mother's care, an immunity from over-work, and the means of education, for that ever-rising growth of population which ere long will form the mass of the nation. By such means we seek to reverse the national condition so sadly bewailed by the Roman poet:—

> "Damnosa quid non imminuit dies?
> Ætas parentum pejor avis tulit
> Nos nequiores, mox daturos
> Progeniem vitiosiorem."

We seek to make the next generation better than the present one. The Political Economy (so-called) which objects to such measures might, with at least equal reason, object to a landowner planting a portion of his rough land with woods, — seeing that the immediate effect must be a diminution alike of his capital and of the profit from his land. He must wait years for a return. But the return will come in his case: and not less surely will it come in the case of a nation which makes a temporary sacrifice of the labour of a portion of its members in order that those members may ere long become better, healthier, and more productive elements of the community than they would otherwise be.

In truth, there is a double gain from a State-policy of this kind: a gain not merely financially—not merely by the population becoming more efficient as agents of production, but also from the higher *morale* which they will acquire, thereby "sweetening the breath of society," and purging the commonwealth of its corrupt parts.

Poverty and crime can never wholly disappear: a large portion of those evils is simply the result of defective organisation: but a still larger portion is the result of vitiated health, unaided ignorance, and bad surroundings. Let us do our best to cure what is curable, and the result will amply repay the momentary sacrifice. England without her "dangerous classes"—without her involuntary paupers, and without the crime begotten of such poverty and of ignorance—would be a glory and a paradise of the earth.

The education of the people, and legislative measures of protection for the children of the poorer classes, are now acknowledged to be an essential part of the duties of the State. They are moral and sanitary agencies of the highest value. But are there not other agencies of a directly money-making kind which may be brought to the help of the weaker classes,—and the adoption of which by those classes may be considerably assisted by the State?

As regards the working-classes, the Co-operative system is by far the best—practically the only direct—means of enabling them to rise above the wants of the hour, by acquiring, in their own small way, reserve-wealth. Mr Gladstone has drawn a distinction between co-operative societies which aim directly at production, such as manufacturing establishments, and others which devote themselves to retail business, in the shape of supplying the members with goods. We fail to see the distinction. In both cases the aim is the same, —namely, to give to the working-classes a part of the profit which otherwise would go to capitalists. Singly,

the working-classes cannot accomplish this: by Co-operation, by the junction of many very small savings, they can. In a Co-operative factory, they obtain for themselves the profits of a master,—in other words, of a capitalist: in a Co-operative retail-store they do the same. In each case, by combining their small savings, they play the capitalist to themselves, and share among themselves the profits. In a factory, they divide the profits of management and of capital, obtaining the whole price for the goods which they produce. In a store, they do the same, by obtaining the goods which they require at cost-price.

The Co-operative system, even when fully developed, will never obliterate the line which separates capitalists and labourers. There will always be men who, either by inheritance or by superior sagacity and prudence, possess a far larger portion of wealth than others; and there will always be a far larger class who, by inferiority of mental organisation, by comparative deficiency of practical intellect or of prudential character, must rely from week to week upon their labour. But the Co-operative system will partially obliterate the hard line which at present separates those classes. The spirit of the British Constitution throws open a career to all men. Even the hereditary peerage, the most exclusive of all our bodies, is annually recruited from the ranks of the people. And any means by which the far lesser change is accomplished of transmuting the wages-receiving classes into men holding a permanent interest in the factory where they work, is not only desirable in itself, but strictly in consonance with the

spirit upon which alike Society and the Government in this country are framed.

The initial difficulties in this, as in all other new developments of finance, are serious. It is only experience which can teach how such improvements may be safely and wisely carried out. If the working-classes, intoxicated by the noble idea of co-operation, were suddenly to rush into the scheme to a large extent, doubtless many miserable failures would ensue. Such a course is to be deprecated, alike in the interest of the intending co-operatives, and also because of the discredit which it would bring upon a cause essentially good.

The best and safest form in which the co-operative system can be worked under any circumstances, and especially at the outset, is when the enterprise is undertaken in concert with a capitalist or large employer. Say that a millowner, reserving two-thirds of the capital invested in his business, resolves to divide the remaining third into very small shares, offered to his workpeople. *All* the workpeople, doubtless, will not at first accede to the scheme: and preparation must be made for this. Say, then, that it is arranged that 10 per cent shall at all times be divided (if the profits reach this moderate amount) among the shareholders—each shareholder receiving 10 per cent on the portion of the capital which he has subscribed,—and that thereafter the surplus receipts be divided equally among all the workpeople, whether shareholders or not. But what if the profits are much beyond this point? It would not, we think, be fair that the whole surplus

above 10 per cent should, if the surplus be large, go to the workpeople alone,—else there would be a cause of dissatisfaction to the capitalists (the shareholders), who might withdraw in order to embark their money and labour in other and more remunerative business. While recognising the claims of Labour, the claims of Capital must not be forgotten. Say, then, that while the profits above 10 per cent are divided equally among the workers (the working shareholders included), this arrangement should only hold good up to the limit of 15 per cent of the profits: any surplus above that amount should be disposed of in such a manner that one-half of it would go to the shareholders, and only the other half to the workers in general (working shareholders included). Above 20 per cent, three-fourths of the profits should be similarly appropriated to Capital alone, and one-fourth to pure Labour. In brief, the shareholders or co-operatives would always divide among themselves the profits up to 10 per cent; any profits above 10 and up to 15 per cent would be divided equally among all the workers, whether shareholders or not; of the profits above 15 and up to 20 per cent only one-half would go to the workers as a whole, the other half to shareholders alone; and of the profits (if any) beyond 20 per cent, only one-fourth would go to the workers as a whole.

Of course the working-classes themselves may form Co-operative Societies, and start factories or other trading-establishments, entirely of themselves, and with their own subscribed capital and combined skill. And doubtless there are some men among the working-

classes who have capacity to administer such establishments successfully. The more of such societies the better. Nevertheless there is a great advantage, especially at the outset, in combining the great employer or capitalist, with his large means, his scientific knowledge, his long experience, and calculating judgment, with the "patient labour" of the less gifted multitude. And in almost every case there would still remain the question (stated above) as to the portion of profits to be divided among the pure workpeople, apart from those who are also shareholders. For it is hardly possible to conceive an establishment in which every employé will also be a co-operative.

There is another most important question which I desire to bring into notice — namely, Credit for the poor. Now, Credit involves two things,—the possession of wealth and the possession of character. Neither of those elements of credit can be known to strangers,—character especially being entirely dependent for its value on the fact of its being known. Now, suppose a small tailor or shoemaker wants a loan. By the system of cash-credits, long-established in Scotland, and known in principle in all parts of the kingdom, he might get a loan from a bank—not on his own character and circumstances as known to the bank, but owing to two men who are well known to the bank becoming security for him. This is a great boon. But in such a form, credit can never be easily or widely obtained. The men who become security in such cases derive no profit from the transaction. They do it, speaking roundly, simply from benevolence. Such a system

cannot go far. Is it impossible to find other means of extending this good work?

The first means is by the establishment of Credit-societies among the working-classes. In such societies each member becomes well known to his fellows; the directing body knows how far he is to be trusted,—which banks do not; and they may give him a loan, which he could not obtain otherwise. Such loans would doubtless be small; but it is small loans only that are needed. Hence the working-classes should organise many such credit-societies,—each of them a local concern, embracing members more or less known to each other. This *knowledge*, in fact, is the important point: for no credit-society should lend to a petty shopkeeper or other person whose character and circumstances are not known to it, any more than a bank would do so.

By means of such loans a small tradesman would, being enabled to buy wholesale, get his raw material cheaper than otherwise,—buying in quantity, and paying, it may be, in cash. Retail-dealers, shopkeepers, also, would thereby be enabled to profit in a similar way.

Credit is the great lever of production. It vastly multiplies the productive and wealth-making power of the individual, by enabling him to obtain from others (who do not trade themselves) wealth which he can employ in trade with a good profit. But the grand difficulty is, that no one lends to the Poor. Wealth obtains credit: Poverty none. To him that has is given. Thus, wealth begets wealth; whereas poverty remains perman-

ently poor. Once make a man a small capitalist, and he will get credit, and his productive powers and wealth may indefinitely increase. But how to give him this start? Among the lower-middle class, it is true, this difficulty is tolerably met in our country. By the admirable system of "cash-credits," whereby money is advanced upon character, independent of capital, poor Scotland has thriven amazingly,—individuals of the lower-middle and even of the working-classes rising into both wealth and social position. Two men become security at a bank, and thereupon credit is given, though the person thus credited has not a penny to start with. To some extent the same beneficial system prevails in England. But the point is, How to do this for the Working-classes as a body,—for the great mass who have no friends in the upper classes to help them, still less any reserves of their own?

We think that this is a problem for the State. We have said that the object of a Government, the duty of the State, is to do for the community what the community cannot do for itself. The task above stated is a work of this kind. Doubtless it is a difficult work to accomplish; but in so far as it can be done, it must be done by the State. By the State, or not at all. The State, as the representative of the Nation, has a direct motive for helping the poor: no individual has. The poor, practically, cannot borrow; the ordinary sources of loans are shut against them. But the State, the nation as a body, is open to them. The State lends to the rich,—not as a private boon, but for draining and other good and useful purposes, important as regards the Nation. But

the State-aid should not stop here. Assuredly it is not less important to lessen the number of the poor, to raise the condition of the working-classes, than to develop the resources of the soil.

Such State-loans ought be made, not to individuals, but to industrial co-operative companies of the working-classes, where numbers may give security for repayment. In fact, roundly speaking, such State-loans must be made to co-operative societies. We do not advocate throwing away money. That would be sheer loss to the State, and no permanent advantage to the poor. But we advocate a system of lending to the labouring-class at the mere cost-price of the loans, even though the State bear the whole cost of the supervising process. We repeat, this is an object of supreme importance; and difficult though its full attainment be, it is worthy of the highest efforts of our statesmen. It is simply money lent by the Nation in order to raise a portion of the community into a better condition. If wisely made, such expenditure will repay itself amply, by producing more national wealth, political contentment, and social happiness.

There is no subject so tempting as this for the ventilation of crude schemes and baseless theories; nor is there any question in which crude schemes and rash theorising are so productive of mischief. The financial danger of such proposals is much the least part of the mischief; for the advocacy of impracticable plans and unattainable objects, in this department of national policy, tends to produce discontentment, jealousies, and heartburnings among the lower classes, in whose interests such schemes are proclaimed. We therefore pro-

pound our views, earnestly indeed, but with diffidence. We do not proclaim them as dogmas,—we submit them as suggestions. We believe that the Government, whether it be Whig or Tory, is as earnest as can be desired to benefit the weaker classes of the community. All that is wanted is to discover practicable methods of accomplishing this object. And the task is not an easy one.

In a country like ours, where there are no State-lands, where every inch of the soil and every right over the waters has long been in private possession, it is impossible to give *Property* to the poor, or to any one, save by taking it from others. The true object of legislation, in this matter, is to increase *Employment.* Do this, and the acquirement of property will follow. Let the State help to place the means of livelihood within the reach of the poor; and at the same time let it facilitate in every way the rise of the better part of the working-classes in the social scale, by enabling them by mutual co-operation, and with new aid from the credit-system, to play the part of masters and capitalists for themselves. We do not mean that they should rise out of their own class into another and higher one,—though it is open to a few individuals to do so; but that the condition of the whole working-class should be raised, —which is a wider and better boon.

In addition to the methods above-stated for improving the condition of the weaker classes, and consequently of the community at large (some of which methods are already in operation), we desire, in con-

clusion, to suggest other work for the State,—work by which the poorer classes will be benefited, while a new means is provided for the development of the national resources.

A grand work lies before our Statesmen,—namely, that of developing the resources of our country, and, by the same process, of converting into agents of production a large portion of our pauper population. These are the two elements which have to be turned to better account than at present, — namely, the unproductive Labour, and the still imperfectly developed natural resources of the Country.

The first of these objects includes the thinning of the ranks of pauperism, and the diminution of the "sunk capital" annually spent in poor-rates. In the new Parliament, where the working-classes will be fully represented, such objects are likely to be carried out with an earnestness unknown before. The working-classes themselves, we believe, have the spirit, as they unquestionably have a direct interest, to check the growth of the idle poor; and probably we may expect that severer measures for this purpose will be adopted than hitherto would have been politic. For a middle-class Parliament to enact stringent laws relating to the idle poor would have excited false and bitter charges of oppression; but laws passed by a Legislature in which the working-classes are fully represented will be open to no such charges or misrepresentation. In all probability we shall ere long see the Apostolic maxim enforced, that if a man is to eat he must work. Involuntary pauperism will be cared for at least as much as at pre-

sent; but self-imposed pauperism—professional mendicancy, the pauperism which becomes a trade, and attaches itself like a gnawing and sapping parasite to the Social body—will, it is to be hoped, be treated with no mawkish sentimentality. The power of the Executive over those voluntary paupers ought, for the sake of the honest poor, and of the community as a whole, to be strengthened; and the stern and righteous fiat may go forth, If a man will not work, neither shall he eat. One of the first steps in this direction should be the rendering more stringent the Vagrancy Laws,—a measure advantageous in itself, and also important as a means of checking the socially vicious practice of indiscriminate alms-giving. Greater powers should also be conferred upon the State for employing able-bodied paupers in productive industry; and in order to give effect to those powers, it is requisite that there should be a consolidation of the various Boards for the relief of the poor.

But, simultaneously with such measures for compelling the idle classes to fulfil their duty as members of the community, the Legislature will require to adopt means for extending the area of work. Despite the perennial drain of Emigration, every year a hundred thousand individuals are added to our population,—all of them competitors for employment,—constituting an addition to our labour-market; so that either the means of employment must be correspondingly increased, or the poor-rates must increase, and the condition of our masses must deteriorate. Doubtless, owing to our expanding trade, the means of employment are yearly

increasing,—yet, judging by the amount of our poor-rates, barely to an equal extent with the growth of the population. But even if the means of employment did increase in proportion to the growth of population, this would only suffice to maintain the existing condition. We are not content with such a state of affairs. And we should be sorry to think that any Minister, or any member of the community, is content. Our extending trade may suffice to give employment to the new competitors for work who annually enter our labour-market; but, as experience shows, no increase of trade suffices to convert any portion of our million of paupers into productive agents.

In order to do this, there must first be the pressure of legislation brought to bear upon our able-bodied paupers; and secondly, the State must find for them new fields of work of a productive kind. The stone-breaking in our poorhouses is absolutely worthless as regards pecuniary return; and the whole system of treating the poor is thoroughly demoralising. The honest poor ask for work, and we only give them alms, — a pittance hardly sufficing to keep soul and body together, while destroying self-respect in the recipient. If we could give productive work to the able-bodied poor, and pay them for it even at a very low rate, we should preserve their self-respect, and also be able to maintain them in a tolerable degree of comfort. As for the professional paupers, they have no self-respect to lose; but at least we may compel the able-bodied portion of them to become agents of production,—thereby lightening the burden of poor-rates, while improving

both morally and physically the condition of those applicants for relief. The point, then, is, to create new fields of employment, especially for unskilled labour, not merely of a temporary but of a permanent kind,—works such as will not only give employment in their construction, but which will also permanently add alike to the wealth of the country and to the area of remunerative work. In what quarters are such new fields of employment to be looked for, and what is to be their character?

The part which the State must play in this matter is of a twofold character,—by Legislation, and also by direct action as an employer of labour. First, as regards what may be called simple Legislation,—which, as we shall proceed to show, is requisite alike as an incentive, and as a facility, for the development of new fields for labour and new sources of national wealth.

It was one of the cardinal duties of the old Persian religion—of that worship of Light, and perpetual struggle against the forces of Evil, which formed the noblest religion of the ancient world—to utilise and beautify the earth, and to keep pure the rivers, the wells, and the waters. We may profitably act upon those injunctions at the present day. One of our great but still unsolved problems is, how to keep clean and healthy our towns, without polluting the rivers, and without wasting the means of enriching the soil. As yet but little progress has been made towards the attainment of this threefold object. The drainage of many of our towns is still most imperfect, so that alike the health and the wealth of the community (and health of itself adds to wealth) are

impaired—are inferior to what they might and ought to be. And even where the drainage is adequate, it is only accomplished by polluting our rivers, and also wasting the manure which ought to be given back to the soil. While admiring the splendid drainage-system now being carried out in London, where miles upon miles of magnificent subterranean culverts are constructed to render clean and wholesome the Metropolis, does it not excite a feeling of wonder and of deep regret to see, as the issue of all this grand work, a vast river of manure daily and hourly pouring itself wastefully into the barren depths of the sea? A Pactolus flowing past us without an effort to extract its golden sands! A vast mine of wealth ceaselessly emptied into the ocean! A gigantic robbery of the soil,—a defrauding of the land of the rich waste which ought to be returned to it! It is as if, in a mighty forest, the fall of the leaf and of the decaying timber were to be intercepted, and the soil were ceaselessly called upon to "Give, give," without any return to it of the wasted elements of its former products.

One great object, then, is, while improving the sanitary condition of our towns, and thereby adding alike to the health, wealth, and happiness of the nation, to return to the soil the precious stores of manure at present poured not only wastefully but injuriously into our rivers. While improving the health of the community, we must simultaneously utilise the sewage, and give back to the soil the fertilising elements which itself has produced. And this second process will suffice to accomplish our third object. For, by so using the sewage, we shall at the same time rid our streams and rivers of

the sterilising pollution at present poured into them. There is no filter like the earth: sewage-irrigation not only suffices to deposit in the soil all the rich particles of the fluid, but also to purify the water ere it is poured into the rivers. Thus we shall add to the supply of pure water, which under the present system of neglect is yearly becoming less adequate to the wants of the population, and also rendering our inland waters again fit to play their natural part as producers of food. It will enable us to stock our rivers and streams with fish. At present many of those streams are rendered barren—are prevented from yielding their natural produce and helping to supply food for the population—owing to their pollution by sewage, as well as by reason of the poison poured into their waters from our factories.

As regards the sea-fisheries on our coasts, the State must impose a "close-time," as it does in regard to our inland waters. There are difficulties, no doubt, in the way of adopting this course, for the facts of the case are as yet but imperfectly known.* Nevertheless such a measure is indispensable in order to prevent the exhaustion of these food-resources of the country, by stopping the murderous capture of gravid fish. It is now admitted that we have overfished the oyster-beds on our coasts,—we have despoiled them ignorantly and recklessly, without taking any care to maintain their reproductive power, much less to extend their area by

* The greatest authority on all questions relating to pisciculture and the development of our fish-supplies, is Mr J. G. Bertram,—who, not only in his valuable work, *The Harvest of the Sea*, but in the leading periodicals and reviews, has ceaselessly urged upon the public the advantage of developing the food-resources of our rivers and waters.

planting new ones: * but an infinitely more serious loss, because affecting the food-supply of the masses, is occasioned by the annual destruction of the female mackerel and herring while in roe.

In these important matters—namely, as regards the sewage, the fertility of our rivers, and of our coast-waters, the only part which the State has to play is that of Legislation. It will not of itself develop those resources—for private enterprise is adequate for this work: but it will clear the way. Especially as regards the utilisation of sewage, Invention must supplement legislation; but legislation will greatly quicken invention by bringing to bear upon it the stimulating pressure of Necessity.

In all these matters, while the State clears the way, private enterprise must do the rest. As regards the utilisation of the sewage, joint-stock companies will be formed for conveying our rich waste to the fields. Moreover, a new field for the use of sewage will be created by the State-works suggested in the sequel. The stocking of our rivers and inland waters with fish—nearly all of those waters being private property—must likewise be accomplished by private enterprise. As regards some of our lakes, companies may be established for the purpose of converting them into fish-farms. History tells us how the Egyptians of old annually raised a large revenue from a single artificial lake, formed by the overflowings of the Nile. In China we see the same thing done at the present day: even the temporarily

* Under the directions of Professor Coste, of the French Institute, a yearly increasing number of oyster-beds are being planted round the French coasts.

flooded rice-fields there are stocked with fish, and yield food to the labourers. Doubtless, if a lake is to be converted into a fish-farm, we must act as we do in all other processes of production. We feed the soil by manure, in order to raise it to its full power of production; and if we want to get the most from farm-stock, we do not leave the sheep and cattle to find food for themselves solely from the hillsides or the uncultivated ground. We must act in like manner if we would develop the food-producing power of our lakes and ponds. Especially in the case of the English and Scottish lakes, whose beds are for the most part rocky, the food-elements which they contain must be increased, by the sowing of water-plants in the shallows, and such-like means, in order that the growth of their marvellously prolific finny population may indefinitely increase. If the large lakes of Great Britain and Ireland were thus cultivated—if our ponds and canals were stocked with carp, our marshes with eels, and our rivers with trout and salmon—the addition thus made to the food-producing power of the country would be far greater than almost any one at present imagines. There is no reason why an acre of water might not be made as productive as an acre of land. Country gentlemen, who have any waste or ornamental water on their estates, should stock it with carp,—if not for the sake of their own tables, for the benefit of the poor of their respective neighbourhoods. And if it be remembered that nearly one-half of our entire population are dependent for food upon the corn and cattle imported from abroad—not to speak of the immense amount of what may be called luxuries, such

as tea, coffee, &c.—the importance of this object can hardly be overrated. It would add alike to the food and to the employment of our people.*

As regards the Land, the action of the State must be of a more direct kind. There are vast natural resources of the country which cannot be turned to account save by the direct action of the State. The works requisite for this purpose are too great to be undertaken by private enterprise. They are either so costly, or they involve so many separate and conflicting interests, or else the return upon the expenditure would be so remote, as to render their execution impossible save by the State—by the Nation as a whole, acting through the Executive.

As an example of this kind, we may particularise the reclamation of the vast waste-lands of Ireland. An immense tract of the central and western area of Ireland, comprising about a million and a half acres, at present exists in this useless condition. Besides the "Bog of Allen," extending in dissevered portions through King's County, Longford, Westmeath, and Kildare, there is a far vaster tract of waste-land lying west of the Shannon in the counties of Galway, Roscommon, and Mayo. Such a work of reclamation may suitably, and we believe profitably, be undertaken by the State. In many cases, the portion of the soil which presents the greatest initial difficulties, and which is the last to be brought

* The marvellous, if not perilous, extent to which our population is dependent upon foreign countries alike for Food and for Employment, and the urgency of developing our own food-resources, was pointed out in my former work (*The Economy of Capital*, pp. 381-408). For the present amount of our Food-imports, see *supra*, p. 55. Even in ordinary years, we import food and food-luxuries to the value of nearly 80 millions sterling.

under cultivation, proves the most productive in the end. This has been the case with all our marshy flats: and we believe it will prove true in the case of the peat-bogs and marshes of Ireland, where deposits of rich material are likely to be found, ready to manure the reclaimed ground; and where in almost every case we may look for an underlying virgin soil, composed of decayed vegetation, which will abundantly repay cultivation.

In the reclamation of those Irish waste-lands, two different processes must be adopted. As regards a great portion of the area, drainage on an imperial scale must be undertaken: works extending over great distances, and passing through the estates of many separate landowners, in order to carry off the sterilising waters from those inland tracts to the sea. And in regard to the whole of this wide region of bog, whether marshy or dry, costly processes of reclamation and cultivation are required. In most parts, the peat must be removed before cultivation can begin; and Science now enables us to turn to profitable uses even this superincumbent mass of sterile soil. In other parts, woods may be planted, which in the course of years will yield an annual revenue in the shape of timber. Any one who visits Dunkeld, and some other parts of the Scottish Highlands, may see what magnificent trees can be grown, and how extensively timber-cultivation may be applied, upon a thin and rocky soil incapable of any other kind of production.

The State, of course, before engaging in those operations, would purchase the area of waste-land which it

proposed to reclaim: a purchase which would cost little, and the payment for which could be made in such a manner as to defer the greater part of the burden until the lands became productive.

Thus, besides obtaining a large and new field for the employment of unskilled labour, and also securing a great future addition to the resources of the country, the State, being in possession of this large tract of reclaimed ground, could try the experiment of leasing the ground in small holdings to Crown-tenants.* This is a measure strongly urged, in some quarters, as a means of improving the social condition of Ireland: and it certainly could not be adopted in a better manner than that which we propose. From the outset of these State-works of reclamation, additional employment would be furnished to the Irish poor and peasantry; and in the issue, a large extent of Crown-lands would be obtained, upon which the experiment of small holdings might be tried in the best form.

Another work, similar in purpose, though widely different in form, remains to be accomplished by the State. The grand obstacle to the growth of this country, in population and national power, is the smallness of our territory,—the limitation imposed upon our growth by the engirdling seas. The greatest boon that could happen to us would be if the sea were suddenly to throw up a broad margin of dry ground all round our coasts.

* It would be a mistake to place the Irish peasants in absolute possession of these small holdings: for, we believe, they would divide and subdivide the soil until they became a population hardly above the condition of paupers even in average years, and sinking into utter pauperism and starvation whenever a bad year came.

Such an ocean-gift, of course, is not be looked for. But a great addition to our resources—alike to the supply of Employment and of Food—would be obtained were the enclosure of land from the sea, from the tidal margins, to be undertaken as an imperial work. Look what Holland has done,—nay, did centuries ago. And if the Dutch—then poor in wealth, scanty in numbers, though indefatigable in spirit—accomplished so much in this respect several centuries ago, what may not the British nation now accomplish, with our vast wealth and super-abundant population, aided by all the engineering science and mechanical appliances which full-grown civilisation places at our disposal?

A glance at the map will show what wide enclosures might be made even on the coasts of England alone. Look at the extensive shallows of the Solway — or Morecambe Bay—of the Wash—of the estuary of the Severn, and at the mouth of the Thames. In the Bristol Channel several miles of sea-bottom, covered in many parts with alluvial mud, could be reclaimed — with great advantage to the navigation, which at present is very perilous. Large enclosures also might be made on the Essex coast, stretching from Southend northwards to the mouth of the Blackwater. This is an area of operations for State-works for years to come. Here, if not elsewhere, is an ample field for the profitable use of all our wasted sewage. Those sandy tracts, left bare, or almost bare, by the refluent tide, might all be enclosed, and added to the productive soil of our little country. The expenditure, it is true, would yield no pecuniary return for wellnigh the lifetime of a gen-

eration: but thereafter almost the whole rent of the land would be *net* profit, and would amply suffice to extinguish the State-loans contracted for the execution of those works. Moreover, even the present generation would benefit largely by the additional employment thus afforded for unskilled labour, and by the consequent thinning of the ranks of pauperism, and decrease of the poor-rates.

Nor would the State be left to bear the whole initial burden of such great and beneficial undertakings. Companies would be formed, undertaking special branches of the work of reclamation, and thereby lessening the task of the State. For example, a joint-stock company has been projected for removing and utilising the beds of peat which at present encumber the surface of the bog-region of Ireland; and doubtless companies would spring into existence, in the wake of the State's operations, to do other parts of the work of reclamation, alike as regards the waste-lands of Ireland and the enclosures to be made from the sea. But the State must take the initiative: it must execute those parts of the works which, either from their costliness, or legal obstacles, or owing to the long time which must elapse before an adequate return on the expenditure is obtainable, cannot be accomplished by private enterprise. A joint-stock company is an ever-changing body, which cannot be expected to undertake the execution of works upon which (as in the case of reclamations of land from the sea) no returns are to be looked for until after the lapse of thirty years—in other words, until the first generation of shareholders has passed away. But the State—

i.e., the Nation as a whole—can afford to wait this time; especially as even the present generation would receive a return for its share of the burden in the lightening of the poor-rates, and in the increased comfort and contentment of the masses.

In the case of the waste-lands of Ireland, the first thing to be done is to make a complete engineering survey, and system of drainage, for the whole area of waste-lands which it is proposed to reclaim. This is indispensable: for if the drainage-plans of any part be made without regard to the requirements of the whole district, the plans first executed may seriously obstruct those to be subsequently carried out,—as was disastrously experienced in the early drainage-works in the districts adjoining the Wash. But, while the engineering plan for the whole area ought to be made complete from the first, it does not follow that the whole plan should be carried out at once. No more work should be undertaken in any year than is sufficient to open a field for the employment of the surplus of unskilled labour which exists in the community,—namely, for the able-bodied poor who cannot find employment for themselves.* Out of regard to financial considerations, also, the work should be executed in parts. If the works

* Sufficient work for our convicts, we believe, might be found without employing them in the works mentioned above. But if any portion of them were so employed, it would be indispensable that these gangs of criminals should be kept distinct from, and subordinate to, the other workers. There should be no degradation for the poor employed on those works,—only a rate of pay so low as to make them return to ordinary employment on the first opportunity. In fact, no money need be given to them at all: an order upon the Government Stores for an equivalent amount of consumable articles would suffice.

were to be carried on at once and simultaneously over the whole area marked out for reclamation, a heavier burden would be imposed on the public than is desirable or necessary. The works, though planned as a whole, should be executed in parts; so that one part may be reclaimed, and rendered productive, before the others are undertaken. This could easily be done. Owing to the different levels, and other circumstances of those waste-lands, the drainage-plans would subdivide themselves into parts,—each of which, as regards its execution, would be more or less independent of the others. In this way the work of reclamation could be carried on gradually,—so as to require neither more labour than our unemployed population can supply, nor more money than can be expended profitably even with reference to the interests of the contemporaneous tax-payers,—*i. e.*, than the public would gain by the diminution of the poor-rates.

The enclosures from the sea, of course, could not be executed in this manner. The whole sea-wall would require to be constructed before any portion of the new land could be turned to account. As regards those enclosures, it is doubtful whether the State should keep the new lands in its own hands,—leasing them to Crown-tenants. Unquestionably the heavy cost of enclosing and reclaiming these lands would be greatly lessened if the State confined its operations to the enclosure and drainage of the area, and thereafter made over the land to joint-stock companies, which should engage to render it productive by the use of sewage and other appliances. If the cost of carriage were not too great,

no plan would be so efficient as to convey to those sandy tracts the peat of the Irish bogs, to be combined with the sewage of the adjoining towns; for peat contains the elements of the richest soil, and nothing so quickly converts it into such soil as the fermentation produced by mixing it with manure.

We must next venture a few words—although merely suggestively, or at best as an outline—with respect to the financial process by which the State should carry out those large works. In the first place, it is to be observed that such works would amply repay the State in future years by the permanent addition which they would make to the field of employment in this country, —thereby sufficing to retain, as tax-paying and wealth-making members of the community, a portion of our people who would otherwise emigrate. These works would also add in an equal degree to the food-producing powers of the country. Nevertheless the future gain is not enough. We do not doubt the patriotic sentiments of the Nation,—we do not doubt that the public would be willing to submit in some degree to financial burdens in order that the prosperity of the country of our children might be increased. Nevertheless, it is desirable to render unnecessary any such sacrifice, however small, of present interests. And we think that the works which we have suggested might be executed without any addition to the taxation, local and imperial, of the country.

The main object, then, to be kept in view is to accomplish the proposed works without adding to the general taxation—local, of course, as well as imperial—of the

country. And the first point to be attained is, that the present cost of those State-works should be compensated by the diminution of the expenditure of "sunk capital" in the form of poor-rates. Conducted on the principles which we have stated, these works would not affect the ordinary labour-market of the country; they would simply take the place of the present useless and demoralising labour in our Unions,—thereby preserving the self-respect of the applicants for relief, while rendering their work a means of repaying the cost of their maintenance. Under the existing system, the labour of able-bodied paupers is virtually wasted. Labour, in fact, at present is imposed upon the paupers simply to deter them from applying for relief. If employed on those State-works, the paupers—the poor who cannot get other work—would be maintained in a state of comfort, very different from their present condition. But, in return, the State would demand from them *work*,—and it would be work which would repay the cost of their maintenance in comfort. When it is remembered that the amount annually raised from the public in the form of poor-rates is about twelve millions sterling,* it becomes obvious that a very small, almost infinitesimal, reduction of that sum would suffice to pay

* The amount of Poor-rates paid in England and Wales alone, in the year 1866, was £9,958,250. But not one-half of this amount ever reached the hands of the poor. Three millions (£2,997,642) were absorbed in Police and County Rates and other expenses "unconnected with Relief." Two millions (2,054,048) were spent in salaries, for lunatic asylums (£566,000), and other expenses "connected with Relief." And 4½ millions reached the hands of the poor,—£1,188,784 in the form of Indoor relief, and £3,196,685 in the form of Outdoor relief.

the interest on the money expended in the execution of these great State-works.

And the interest on that sum is all that we have to do with. The future profit which will accrue from the works of reclamation will in the end suffice to pay-off the capital borrowed in order to execute them. In the case of the Irish bog-lands and wastes, this will occur at no distant period; but probably a generation must pass away before the proposed works of enclosure from the sea can become directly remunerative,—*i.e.*, before the return will suffice to repay the capital expended upon them. Although the State were to borrow at the present rate of interest on our State-Debt—namely, about $3\frac{1}{5}$ per cent—we believe no additional burden would be imposed upon the community. Such State-works might surely be expected to lessen the poor-rates to the extent of one-hundreth part (1 per cent): this, on the 12 millions, would be £120,000 a-year. Now, £120,000 a-year would be the interest on four millions sterling; and we do not think that more than this sum would ever be required at once. This would certainly be the case in regard to the Irish waste-lands; for the land so reclaimed would speedily become productive,—yielding a revenue which would at once suffice to pay a portion, and very soon the whole, of the annual interest on the expenditure.

But in order to minimise the present charge for interest upon this expenditure, the State should borrow in such a manner that the burden would be less on the present generation than on the succeeding one: for example, by contracting a loan at 3 per cent *at most*,—

which could easily be done, on the condition that at a given period the bondholders should be paid a larger sum than they subscribed. Say that the loan were contracted at 3 per cent, and that the subscribers of £100 were to be repaid £125 at the end of 25 years; this would virtually be borrowing at $3\frac{2}{3}$ per cent, although a part of the payment would be postponed to future years, when the State-works would become remunerative. In the case of the Irish waste-lands, the loan need not be for so long a period, and consequently the ultimate premium to be paid on the amount borrowed would be proportionately less. Nor is it requisite that the given time for the repayment of these loans should be absolutely adhered to. It would be difficult to ascertain correctly at the outset, the date at which the reclaimed lands would yield a certain annual sum. But this does not matter. A time should be fixed for the repayment of each loan—say of £125 for every £100 subscribed: but the State might reserve to itself the right to pay off the loan sooner, or later, according to circumstances. If the loan were paid off sooner than the stipulated time, the bondholders of course would receive somewhat less than £125 for each £100. If it were paid off later than the stipulated time, then the State would on each year after that date have to pay interest on £125 instead of on £100. This would in no way alter the financial character of the compact, either as regards the State or the bondholders. The security of the State being absolutely perfect, the bonds would sell at nearly (if not quite) their full value from the outset; and they would do so likewise if repay-

ment were postponed on the above-mentioned terms. In fact, the bonds, whether paid sooner or later, would always bear (nearly, if not quite) the same value; accordingly they would sell at the same price, *cæteris paribus*—*i. e.*, in the same condition of the money-market.*

If this plan of State-works were carried out, the State would proceed to contract new loans in proportion as the first loans were paid-off. Hence, as a matter of fact, there would be little or no payment of money in discharge of those loans. The public would take up the new State-bonds in lieu of the old ones: that would be all. But it would be exceedingly desirable, as a matter of accounts, that the loans contracted for each successive undertaking should be kept separate,—in order that the history of each investment might be recorded. Each loan should be kept distinct, and paid-off from the proceeds of the particular lands upon the reclamation of which it was expended.

It is important to add that these loans for Public

* As the State-loans would be of small amount—probably never at any time exceeding four millions,—they might all be taken up by the Insurance Companies and other parties desirous of making a permanent investment in such State-securities, which would yield a slightly greater return than ordinary Consols. To such permanent investors, a State-bond for £100 yielding annually 3 per cent of interest, and repayable by £125 twenty-five years after date, would be equal to value to a bond bearing 3¾ per cent all through the period. On the other hand, if such bonds (like ordinary Consols) were constantly changing hands, their current value in the early years would be less than the full value,—seeing that any person who merely held them for a year would only get 3 per cent interest; whereas in the later years their value would exceed their average value for the whole period,—owing to the approach of the stipulated time at which they are to be paid-off at £125 for every £100.

Works should form a distinct and separate portion of the National Debt. They ought not to be raised in the form of Consols,—but as a new kind of State-bonds. It would be a double mistake to make such loans simply an addition to the Funds: first, because we propose that they should be borrowed at a lower rate of interest than that payable on the Funds,—the difference being made up in the form of a deferred payment. And secondly, because if they were mingled up with the main body of the National Debt, it would be much more difficult to pay them off. It is the magnitude of our 3 Per Cents which constitutes the most serious obstacle to dealing with them. They cannot be dealt with in part. Any proposal for converting them into another kind of stock must be made to the whole body of Fundholders. Hence any attempt to reduce the rate of interest upon them—say by converting them into 2½ per cent stock—must of necessity fail: for even though nine-tenths of the Fundholders were willing (which, however, they are not likely to be) to submit to this change, the refusal of the others would prove fatal to the scheme,—seeing that, in order to carry out the scheme, the Government would have to raise a new loan of 70 millions in order to pay-off even so small a minority as we have supposed of objecting Fundholders. Moreover, even if no attempt were made to reduce the value of the 3 Per Cents,—though it were merely desired to convert them at their full value into terminable annuities, the scheme is rendered impracticable by the magnitude of the amount (780 millions) to be dealt with, even though all the Fundholders were willing to accept the proposed terms.

Throughout this work, we have strenuously opposed all needless State-intervention in industrial enterprise. It is only where a great national work has to be accomplished, which private or local enterprise cannot undertake, that the State should intervene. The two great requirements of State-intervention are: first, that the work should be of national importance, yet beyond the sphere of private enterprise; and secondly, that the nature of the work should be specially fitted for the employment of unskilled labour,—so as to present a field for the profitable employment of the able-bodied poor who cannot get other work. In both of these respects, the great tasks which we have proposed for the State are perfectly suitable. In the same category, also, may be included the construction of railways in Ireland, with the view of opening up districts which but for State-help must remain secluded and unprogressive. Such State-help to be given (as in India) in the form of a guaranteed rate of interest upon the expenditure.*

The construction of railways and reclamation of the waste-lands of Ireland are works which ought immediately to be undertaken. The enclosures from the sea, on the other hand,—being a work which would be much more tardily remunerative,—ought to be kept in reserve for seasons of exceptional distress. Nevertheless, even in the latter of these cases, the surveys, plans, and estimates ought to be made at once, in order that the works might be undertaken promptly, when occasion required, instead of losing precious time when the distress is upon

* See also p. 564.

us, by having to do then the preliminary work which may be advantageously performed at present.

An expenditure for those objects would be far more profitable than devoting an equal sum to the diminution of the National Debt. In truth, it would have been much better, and wiser on the part of Parliament, to have devoted the half-million now set apart for extinguishing a portion of the Debt, to the execution of such works as we have named. As a rule, money cannot "fructify" in the hands of the State, because the State does not *trade*. But in this exceptional case, the State would, for the sake of the nation, engage in industrial operations: and although these operations would probably give no direct gain to the State, even after the lapse of many years—direct gain indeed forming no object of the enterprise, — yet the money expended would "fructify" as regards the Nation, by adding to the resources of the country, and moreover would benefit the State indirectly by eventually increasing the productiveness of taxation.

Ours is a very small country. And the greatest object of our Statesmen should be to compensate our geographical insignificance by developing to the utmost alike the natural resources of the Country and the productive powers of the People. The first step towards the attainment of this grand object of national policy is to diminish the numbers of our pauper-class, and turn to remunerative account the labour of those who remain. At present, one-thirtieth part of our population are not only non-productive, but a positive burden upon the wealth, and a drawback upon the general welfare of

the community. Every day in the year, there is a million of persons on the poor's-roll; of which number at least 150,000 are able for work. A vast Army of Industry, at present turned to no account. Even if one-third of those able-bodied paupers were employed on works which would simply repay the cost of their maintenance, a sum might annually be saved amply sufficient to pay the interest on the State-loans required for the execution of such works; while these would not only give employment to those paupers, but would permanently increase the field of employment, while adding to the productive area and wealth of the country. We should turn to account a portion of our non-productive Labour, while extending the natural resources of the Country.

The other great object of our national policy should be to develop to the utmost the productive powers of our population. Despite every means which may be employed to extend the productive area of our country, our population must ever remain small compared to that of the great empires now rising around us,—small also compared with the additions annually made to our population. Emigration must still continue to draft away from us a large portion of our national growth. Hence it is a matter of the utmost urgency that we should make the most of those who remain. If we are not to decline—rapidly, and for ever—in the scale of nations, we must develop to the utmost the physical, intellectual, and moral condition of our people. We must improve the condition of the lower classes in order that Society may be happier and the political fabric stronger.

We must develop their intellect, their productive power, in order that the same amount of population may suffice to produce a greater amount of wealth. As regards productive power, we must seek to make every man of our labouring-class in the future worth two in the past. Just as, by the appliances of science, we have doubled the motive power of the steam-locomotive in the lifetime of a single generation, so must we seek, by means of education and culture, to develop the highest latent powers of our people. And progress in that form is, happily, almost illimitable. The area of our little isles may remain as they are, fixed by the surrounding seas; but the amount of productive force which may be evolved from our population may increase from year to year in a manner which would appear marvellous to ourselves if we could witness the results in the generation to come. Human power, in truth, is the most expansible of all forces: and by the earnest development of that power, our islands, geographically so small—a mere speck on the map of the world—may steadily and marvellously expand in resources, like the magic tent of the fairy tale, which was large enough however numerous the persons who entered it.

A great future is still before England. Let the State rise to the full discharge of its functions. Now more than ever the State is simply—the Nation acting for itself. Henceforth the State will be possessed of double strength,—of powers equal to the performance of every work required of it in the interests of the nation. Let it use those powers wisely and fully, and the British Isles will rise into new power and hitherto unequalled prosperity.

APPENDIX

ANNUAL ABSORPTION OF SPECIE.

(See p. 43.)

Gold and Silver coined at the Mint.			Light Coin withdrawn from Circulation.		
Years.	Gold.	Silver.	Years.	Gold.	Silver.
1843	£6,607,849	£239,580	1843	£2,559,893	£107,000
1844	3,563,949	610,632	1844	3,314,122	56,000
1845	4,244,603	647,658	1845	718,075	23,900
1846	4,334,911	559,548	1846	609,143	18,000
1847	5,158,439	125,730	1847	660,477	14,500
1848	2,451,999	35,442	1848	800,820	54,750
1849	2,177,955	119,592	1849	611,139	135,100
1850	1,491,836	129,096	1850	465,633	150,000
1851	4,400,411	87,868	1851	641,636	100,000
1852	8,742,270	189,597	1852	430,608	48,200
1853	11,952,391	701,545	1853	403,786	22,000
1854	4,152,183	104,480	1854	474,766	16,000
1855	9,008,663	195,510	1855	379,563	63,000
1856	6,002,114	462,528	1856	419,121	74,000
1857	4,859,860	373,230	1857	511,000	92,568
1858	1,231,023	445,896	1858	393,000	67,500
1859	2,649,509	647,064	1859	334,000	60,000
1860	3,121,708	218,403	1860	374,000	113,000
1861	8,190,170	209,484	1861	581,000	97,600
1862	7,836,413	148,518	1862	618,000	135,000
1863	6,607,456	161,172	1863	482,000	102,800
1864	9,535,597	535,194	1864	456,000	123,500
1865	2,367,614	501,732	1865	645,000	93,000
	£120,689,928	£7,449,499		£16,882,790	£1,767,418

Amount of gold and silver coined at the Mint between 1843 and 1865, ... £128,139,427

Amount of light gold and silver coin withdrawn from circulation during the same period, . . . 18,650,208

£109,489,219

Showing an average addition of £4,760,400 a-year to the stock of coin in the country,—which would not be needed if small notes were allowed to be issued.

STATISTICS OF THE CRISIS OF 1866.

(See Chapter XIV.)

I.

THE BANK OF ENGLAND.

A glance at the position of the Bank of England immediately before the crisis, during the crisis, and six months afterwards, will show how great was the convulsion, and how striking have been the vicissitudes. On the 9th of May, the day before the outbreak of the Crisis, the position of the Bank was as follows :—

Note-Circulation.	Gold in both Departments.	Reserve. Notes and Coin.	Loans and Discounts.	Bank-rate.	Private Deposits.
£22,344,395	£13,156,140	£5,811,745	£20,844,217	8 p. c.	£13,515,537

On the afternoon of the very day after these returns were drawn up, the great firm of Overend, Gurney, & Co. suddenly stopped payment; and on the 11th, Panic reigned supreme in the City. Mark the consequences, as shown in the next returns of the Bank of England (May 16) :—

Note-Circulation.	Gold in both Departments.	Reserve Notes and Coin.	Loans and Discounts.	Bank-rate.	Private Deposits.
£26,120,995	£12,323,805	£1,202,840	£30,943,259	10 p. c.	£18,620,672

Finally, let us show the position in which the Bank was left after the Crisis was over. The Bank-returns for 28th of November 1866 were as follows :—

Note-Circulation.	Gold in both Departments.	Reserve Notes and Coin.	Loans and Discounts.	Bank-rate.	Private Deposits.
£22,486,750	£18,175,570	£10,358,918	£19,186,008	4 p. c.	£13,515,537

Thus the first effect of the Crisis in May was to add 10 millions (50 per cent) to the Bank's loans and discounts; fully 5 millions to its private deposits; and nearly 4 millions to its note-issues. Hence it appears that of the 10 millions of advances required from the Bank, half of that amount was not withdrawn from the Bank at all: it simply remained at the credit of those parties who had got the loans. Of the remaining 5 millions, £3,776,000 were taken from the Bank in the form of notes, and £810,000 in coin. It is also to be noted (as shown by the return obtained by Alderman Salomons) that of the 3¾ million of notes thus withdrawn, the greater part were large notes,—not meant for currency, but either for hoarding on the part of the public, or for the payment of deposits by the banks.

These facts throw great light on the nature of the difficulty experienced by the Bank in May. The demands upon it were of two kinds: (1) From merchants who, owing to the stoppage of Overend's and other establishments, and the general cessation of discounting by the London banks, could not get their usual accommodation from the old quarters, and had to take their securities to the Bank to be converted into banking-currency, or at least into banking-credit. But (2) by far the larger part of the extra demand then made upon the Bank of England came, not from the public, but from the other banks. Many of these establishments had to withstand a "run" for deposits, which they could only meet by suddenly converting their assets into currency to a much larger extent than usual. And this could only be done by taking these assets to the Bank of England, which is the only establishment which is permitted by law to increase its note-issues. The requirement of the banks was twofold. In the first place, they had to meet payment of the cheques drawn upon them and passed through the Clearing-House: and as the settlements in the Clearing-House are made by drafts on the Bank of England, the banks had to increase their deposits at the Bank, to meet the exceptional demand to which they might be exposed. No more currency was required for this: neither did it involve any withdrawal of capital from the Bank. On the contrary, as we have seen, the only effect of this was to add fully 5 millions to the private deposits in the Bank—which doubtless shifted about a good deal from one bank's account to another's, in consequence of the "clearing" operations, but the whole of which remained in the Bank and strengthened its position greatly. But, secondly, while adding to their credit or deposits at the Bank of England, the London banks had also to meet the crisis by other means. While they had to provide for the extra run made upon them through the Clearing-House by increasing their credit at the Bank, they had at the same time to meet the run for deposits made upon them "over the counter," by laying in a much larger stock of currency than usual. Hence, beside

adding largely to their deposits in the Bank of England, they had to withdraw from the Bank some 3¾ millions of notes and £800,000 in coin.

These operations, by which the banks supplied themselves with currency during the Crisis, were simply temporary exchanges of capital for currency. The banks took a portion of their negotiable assets (Government Stock, bills, &c.) to the Bank, and obtained a supply of banking-currency in exchange, by which they might meet the unusual demand for cash-payments made upon them by their depositors.

Probably at least three-fourths of the increase in the Bank's loan and discount business in May came from the other London banks; the remaining fourth from persons who could not get their bills discounted in the old quarters (owing to the bank-suspensions and general stoppage of discounts), and who accordingly had to apply at the Bank of England.

The effects of this immense increase of business, contemporaneous with an exorbitant rate of interest, are visible in the large profits made by the Bank during the Crisis. The undivided profits at the close of the half-year ending September 5, 1866, amounted to *four millions* (£3,987,416), the highest point ever reached: and the net profit on the half-year was £975,655, the largest ever made by the Bank. Moreover, if the weekly gains of the establishment be examined, it will be found that these were fully twice as great during the period of monetary distress as in the remainder of the half-year. During the fourteen weeks when the rate of discount was 10 per cent, the Bank's profits were £679,000, against only £300,000 in the other twelve weeks.

The following have been the extraordinary changes in the Bank-rate since the beginning of May 1866:—

May	1, 1866,		6 per cent.
,,	2, ,,	raised to	7 ,,
,,	8, ,,	,,	8 ,,
,,	11, ,,	,,	9 ,,
,,	12, ,,	,,	10 ,,
Aug.	16, ,,	reduced to	8 ,,
,,	22, ,,	,,	7 ,,
,,	30, ,,	,,	6 ,,
Sept.	6, 1866,	reduced to	5 per cent.
,,	27, ,,	,,	4½ ,,
Nov.	7, ,,	,,	4 ,,
Dec.	18, ,,	,,	3½ ,,
Feb.	6, 1867,	,,	3 ,,
May	30, ,,	,,	2½ ,,
July	24, ,,	,,	2 ,,

While the Bank-rate was thus falling, the gold in the Bank steadily increased. On August 2, 1866, the gold in both departments was £13,156,140. On Sept. 18, 1867, the gold amounted to £24,498,447,—the highest point ever reached in the Bank's history.

II.

EXPORTS AND IMPORTS OF SPECIE.

Taking Gold and Silver together, the exports and imports of the precious metals in the months previous to, during, and after the Crisis, were as follows :—

	Imports.	Exports.	Excess of Imports.
Jan. to June 1866,	£16,603,137	£11,122,561	£5,480,576
June to December,	17,684,000	10,448,126	7,235,874
Jan. to June 1867,	9,974,850	6,255,242	3,719,508

Taking Gold alone, the statistics for the same periods have been as follows :—

	Imports.	Exports.	Excess of Imports.
Jan. to June 1866,	£12,427,886	£7,355,854	£5,072,032
June to December,	11,081,755	5,386,205	5,695,550
Jan. to June 1867,	6,337,561	3,220,083	3,116,478

Here, then, is a marvel. Less gold has been added to the stock in this country during the first six months of 1867 than in the same period of 1866 ; yet the gold in the Bank of England is enormously larger in amount than it was then,—even though the bank-rate in the first half of 1867 has been only 3 and 3½ per cent, while in the same period of 1866 it ranged from 6 to 10 per cent. Though the influx of gold from abroad has actually been less during these six months than during the same period of 1866, the stock of gold in the Bank has increased enormously, whereas during the same period of 1866 it remained nearly stationary. How is this to be explained? It must be due to the fact that much less gold has been needed for internal circulation. The ebb and flow of the internal gold-circulation is a most important matter, deserving far more attention than has yet been given to it.

During the last three years the movements of specie have been as follows :—

		1865.	1866.	1867.
Year ending Nov. 30.	Imports,	£13,172,852	£22,345,793	£14,235,384
	Exports,	6,670,376	12,634,495	7,026,888
Excess of Imports,		£6,502,476	£9,711,298	£7,202,496

We may add that in the twelve months ending Nov. 30, 1866, 8½ millions of the gold exported from this country went to France.

III.

THE STATE OF TRADE.

The amount of our Home trade it is impossible to ascertain ; but our Foreign trade, as shown by the Exports and Imports, during the last year and a half, has been as follows :—

Jan. to August 1866.		Sept. 1866 to June 1867.	
Exports, . .	£125,200,000	Exports, . .	£151,175,000
Imports, . .	155,800,000	Imports, . .	188,398,000
	£281,000,000		£339,573,000

From these statistics of the Board of Trade, it appears that during the first eight months of 1866 our Foreign trade amounted on the average to upwards of 35 millions a-month ; whereas during the following ten months the monthly average has been only 34 millions, although the normal condition of our trade is a steady increase from year to year. And the returns continue to decline.

IV.

THE BANKS OF ENGLAND AND FRANCE.

The object of raising the Bank-rate, we are told, is to check the withdrawal of gold, and at the same time to attract gold from other countries. But the facts contradict this view of the matter very strongly. During the months of May, June, and July, specie accumulated steadily and enormously in the Bank of France, which charged only 3½ and 4 per cent ; while the bank of England, which charged 10 per cent, found its stock of gold no greater on the 2d of August than it had been on the 3d of May :—

Week ending	Bank of England.		Bank of France.	
May 3, ..	£13,509,000 ..	7 per cent	£21,080,000	
,, 10, ..	13,156,000	..	20,800,000	3½ per cent
,, 17, ..	12,323,000	..	20,600,000	
,, 24, ..	11,857,000	..	21,480,000	
,, 31, ..	11,878,000	..	23,120,000	
June 7, .	13,278,000	..	24,080,000	
,, 14, ..	14,481,000	..	24,520,000	
,, 21, ..	14,851,000	10 per cent	25,080,000	4 per cent
,, 28, ..	15,042,000	..	26,000,000	
July 5, ..	14,876,000	..	26,720,000	
,, 12, ..	13,993,000	..	26,280,000	
,, 19, ..	13,645,000	..	26,880,000	
,, 26, ..	13,716,000	..	27,600,000	3½ per cent
Aug 2, ..	13,793,000	..	28,270,000	

The logic of these facts is unanswerable. Here are two great banks, within twelve hours' distance of one another—one of which holds 21 millions of specie and lends its currency to the public at 3½ per cent, while the other has less than 13 millions of specie and charges 7 per cent. According to the theories which have so long been held sacred, such a condition of things ought to have been impossible. Only a few months before, Baron Rothschild had declared to the French Government Inquiry that if the Bank of France were at any time to lend its money at 2 or 3 per cent below the banks of other countries, it would forthwith be drained of its last sovereign. In spite of this dogmatic theorising, at the beginning of May 1866 we beheld the Bank of France charging only half as much for its loans as the Bank of England, yet no drain at all set in from the former bank to the latter. Although within a few hours' distance, the specie remained unmoved at Paris, while on this side of the Channel the public was forced by the Bank to pay 7 per cent instead of the 3½ in France.

According to the so-called established theory, such a position of affairs was an impossibility,—but here it was. Moreover, what happened when the terrible Crisis began? Instead of disappearing, when the Bank-screw was still further put on, the difference between the two neighbouring Banks only grew greater and greater. While the Bank of England charged 10 per cent for three months, with no result in increasing its stock of gold, the specie in the Bank of France shot up from 21 to 28¼ millions sterling, while its rate of discount was only from 3½ to 4 per cent. In fact, as is well known, so totally inefficacious was the raising of the Bank-rate, that specie actually flowed from England to France, although the rate was 300 per cent higher in the former country than in the latter.

A comparison of the average rate of discount charged by the Banks of England and of France shows that the average has been higher in this country than in France during the last fifteen years. The fluctuations in the rate of discount also, during the same period, have been far more frequent and severe in this country than in France.

During the last twenty years, since the passing of the Bank Act of 1844, the Bank-rate in England has been progressively rising:—

From 1845 to 1849 the average rate was	£3 11 7
From 1850 to 1854 it was . .	2 5 11
From 1855 to 1859 it was . .	4 11 8
From 1860 to 1864 it was . .	4 15 3
And to 1865 it was . .	4 16 0

But it is not the higher *average* rate that constitutes the evil of the Bank Act, but the sudden, frequent, and extreme fluctuations from the highest to the lowest rates which prevail under its operation.

V.

THE ENGLISH BANKS OF ISSUE.

Whether or not the note-circulation of the English provincial banks is at present adequately secured, is a question fairly open to discussion; and in the present work, we have shown how it may easily be placed on a more perfect basis. Nevertheless it is due to them to say that those banks passed through the late Crisis most successfully. Indeed, their condition during the stormy months of May and June 1866, contrasted favourably with that of the Metropolitan banks and discount-establishments, not a few of which went down before the storm. A recently published Parliamentary return throws important light on this question; and the unimpeachable statistics which it contains certainly free the English provincial banks from a most serious charge, brought against them by the late Chancellor of the Exchequer, during the debate in the House of Commons raised by Mr Watkins on the disastrous crisis of 1866.

In his speech on that occasion, Mr Gladstone charged the provincial banks with having largely contributed to the exhaustion of the statutory note-issues of the Bank of England. He said that the note-circulation of the provincial banks became discredited, and that, in consequence, they had to withdraw a million sterling of notes from the Bank of England to give in exchange for their own discredited notes. This statement, certainly, was not in accordance with any intelligence published during the Crisis either in London or in the provinces. It was an inference which Mr Gladstone drew from the official returns of those banks and of the Bank of England. He saw that between the beginning of May and the end of July, the note-issues of the provincial banks decreased to the extent of nearly £900,000 (which Mr Gladstone made "fully £1,000,000"); and he hastily jumped to the conclusion that a corresponding amount of the notes withdrawn from the Bank of England was required and taken by the provincial banks to give in exchange for their own notes brought to them to be cashed. He did not prove that £1,000,000 of the notes withdrawn from the Bank of England actually were taken by the provincial banks; nor are there at present any published statistics to show whether or not this amount of the Bank's notes were taken by those banks. But what is now manifest is, that whether or not this amount of notes were absorbed by the provincial banks, they were certainly not taken for the purpose which Mr Gladstone imagined, and that there is no foundation for the charge which on this hypothesis he brought against those banks of issue.

The peculiarity of the crisis of 1866 was, that the monetary difficulty was not occasioned by the note-circulation of any bank of issue falling into discredit, but owing to a great run for deposits upon nearly all the Metropolitan banks. The public suddenly withdrew from the London banks an unusually large amount of their deposits, and kept the amount (in notes) in their own hands, or for their own use. The consequence was that, at the height of the panic, nearly four millions in Bank of England notes were hoarded,—partly by the public, but partly also by the banks themselves, which were apprehensive of a continuance of the run upon them, and which accordingly laid-in an extra supply of notes to meet this possible emergency. This was the true cause of the great withdrawal of notes from the Bank of England. These notes were not required to give in exchange for other bank-notes, but to pay out to panic-stricken depositors, and also to supply the place of the partially discredited commercial currency (*i.e.*, bills). Hence, as the return obtained by Alderman Salomons shows, by far the greater part of the increased issues of the Bank of England at that time were in the form of large notes, suitable for the payment of deposits. The extra £3,776,000 withdrawn from the Bank of England during the panic week was composed as follows :—

Denomination of Note.	May 9.	May 16.	Increase.
£5, ...	£3,063,000	£3,711,000	£648,000 equal to 8 per cent.
£10, ...	4,299,000	4,876,000	577,000 ,, 13 ,,
£20 to £100, .	6,482,000	8,185,000	1,703,000 ,, 26 ,,
£200 to £500, .	1,798,000	2,337,000	539,000 ,, 30 ,,
£1000, . . .	1,703,000	2,012,080	309,000 ,, 18 ,,

Here it appears that upwards of 80 per cent of the increase was in notes of £10 and upwards, and rather more than 67 per cent in notes of £20 and upwards. As the *Economist* justly observes, "This enables us at once to determine the purpose for which the great demand on the Bank of England was made. The demand for notes above £20 could not be to supply the place of the country circulation, which consists wholly of £5 notes and £10 notes. A £200 note or a £1000 note would, in a circulation run, be wholly useless. All large notes—all above £20—may be assumed to be taken for deposits only. Many of the £5 or £10 notes *may* have been taken out for deposits also, but the higher denominations *must* have been so."

There is another point in Mr Gladstone's statements which deserves elucidation. He said—"If the country bank circulation had been in a satisfactory state, it is evident that not only the notes of the Bank of England, but those of the country banks themselves, would have been largely drawn upon. Instead of that, however, we have seen the country bank circulation diminished by not less than £1,000,000."

Passing by the exaggeration of the diminution, let us consider the substance of the statement. In the first place, it is true that the issues of the country banks at the commencement of the Crisis were below the full amount which these banks are allowed to issue. But the authorised issues of the country banks amounted only to £7,250,000; and this was divided among no less than 190 banks, giving barely £38,000 to each bank. And each bank is bound under a penalty never to exceed the statutory amount of its issues: so that each of these 190 banks, some of which have branches, must always keep considerably below the statutory amount, as a necessary precaution against a momentary excess. Hence a considerable portion of the "fixed issues" of these banks is practically unavailable. As a matter of fact, the highest point to which the issues of the country banks have reached of late years was six millions, in November 1865—at which time their legal power of issue was £7,365,000. As the number of the country banks of issue was at that time 194, this amount of notes in circulation left to each bank on the average only £7000 of its notes in reserve; so that they could not keep their active circulation at a higher point without running the risk of exceeding their statutory amount of issue. Since then, owing to the Provincial Bank of England resigning its power of issue, the legal power of the country banks to issue notes has been considerably reduced. On May 1866 it stood at the amount of £6,814,000; and as at that time the active circulation of these banks amounted to £5,568,000, their note-issues *were then at the very highest amount they have ever felt themselves at liberty to issue*,—the average reserve-power of each of those banks to issue notes being only £6550. Hence Mr Gladstone's averment that they might have largely increased their note-circulation, if it had been in a satisfactory condition, when the Crisis occurred, is a mistake. The note-circulation of the country banks was already at as high a point as it was safe for them to issue, unless they risked incurring the penalty attached to their violation of the Act of 1844.

But acknowledging this — admitting that the increase of issues which Mr Gladstone says would have been natural in the circumstances, was practically impossible,—the second point is, How are we to account for the *decrease* in their note-circulation which unquestionably took place? Mr Gladstone says that this diminution was owing to the notes of these provincial banks falling into disrepute, and being replaced by Bank of England notes. Now, apart from the counter-evidence furnished by the Parliamentary return quoted above, the incorrectness of Mr Gladstone's statement is obvious from the following facts. In the first place, the diminution of the note-circulation of the provincial banks did not take place suddenly, and at the height of the Panic,—as it would have done if it had been occasioned by the public losing

faith in the notes; but drooped gradually week by week after the panic was over,—just as the note-issues of the Bank of England did. Secondly, if Mr Gladstone's statement were correct, the issues of the Bank of England should have increased *pari passu* with the diminution in the circulation of the country banks: whereas the fact was just the opposite,—the note-circulation of the Bank of England diminishing simultaneously with that of the country banks:—

Bank of England, May 16,	£26,121,000	Country Banks, May 12,	£5,568,744
„ „ July 25,	25,263,000	„ „ July 21,	4,700,219
Decrease, . .	£858,000	Decrease, . . .	£868,525

The explanation of the fact upon which Mr Gladstone raised his mistaken hypothesis is easy, and obvious to any man conversant with such matters. The decrease in the circulation of the country banks was caused not from their notes becoming discredited, but from a decrease in the trade of the country, and consequently of the business of the banks. As a natural consequence of the high Bank-rate, the commercial and manufacturing classes contracted their operations; less currency was needed in the payment of wages, &c., and consequently fewer notes were taken from the banks. This diminution of trade is shown by the following official statistics:—

	May.	June.	July.
Imports, . .	£23,224,762	£23,243,701	£19,597,929
Exports, . .	15,870,131	14,630,120	14,957,834
	£39,094,893	£37,873,821	£34,555,763

It is also worthy of notice that even if trade had remained as active as before, the tendency of the note-circulation of the country banks would have been downwards. For, throughout the north of England (as in Scotland) the rent-term occurs in the middle of May—when more currency is always required: so that a slight diminution of the country note-issues was only what was to be expected after the middle of May, apart from the depression of trade which followed the panic. In short, one might as justly say that the diminution of the note-issues of the Bank of England after the month of May was "owing to its note-circulation not being in a satisfactory state," as to make a similar charge against the country banks of issue.

VI.

Overend, Gurney, & Co.—At the time of its stoppage, the liabilities of this great company amounted to £18,728,000. Its subscribed capital was 5 millions; and the portion paid-up (its trading-capital)

was 1½ millions sterling. All the creditors will be paid in full, but the loss to the shareholders will be about 3 millions sterling.

The Bank of London. — Subscribed capital, £800,000 ; paid-up capital, £400,000. Liabilities at time of stoppage (26th May), £3,541,532. This Bank was thoroughly solvent, and only failed because it could not get its assets converted into currency with sufficient promptitude to meet the "run" upon it.

The Consolidated Bank.—Subscribed capital, £1,500,000 ; paid-up capital, £600,000. The momentary suspension of this Bank was owing solely to a technical difficulty, arising out of its arrangement with the Bank of London.

English Joint-Stock Bank.—Subscribed capital, £1,000,000 ; paid-up capital, £400,000. This Bank also was perfectly solvent, but, like the Bank of London, failed owing to its being unable to convert its assets into currency with sufficient promptitude to meet the "run" for deposits. It is believed that the loss which will accrue to the shareholders will be caused simply by the effects of the sudden stoppage.

Agra and Masterman's Bank.—Subscribed capital, £3,000,000 ; paid-up capital, £1,500,000. This Bank, like the others, failed owing to its inability to convert its assets into currency with sufficient promptitude to meet the demands of its panic-struck depositors. It has since been re-established (under its old name, the Agra Bank), and is carrying on business with success.

European Bank.—Subscribed capital, £2,146,700 ; paid-up capital at time of failure, £644,490. The creditors will be paid in full ; but it is expected that nearly all the subscribed capital will be lost ere the liquidation is completed. The liabilities at the time of the failure (19th May) amounted to £2,700,000.

Imperial Mercantile Credit Association. — Subscribed capital, £5,000,000 ; paid-up at time of failure, £500,000. The creditors will be paid in full ; but it is expected that nearly all of the subscribed capital will be lost.

Joint-Stock Discount Company.—(This company failed three months before the Crisis occurred, but we may include it in the list.) Subscribed capital, £2,000,000 ; paid-up capital at time of failure, £800,000. The entire capital has been lost, but it is hoped that all the creditors will be paid in full.

Barned's Bank.—Subscribed capital, £2,000,000 ; paid-up capital at time of failure, £400,000. The shareholders will lose the whole amount of the subscribed capital, and it is not expected that the creditors will be paid in full.

Contract Corporation.—The whole of the subscribed capital of this company (£2,000,000) has been called up, yet the dividend for the creditors is expected to be very small.

International Contract Company.—The whole subscribed capital of this company (£2,000,000) has been lost, and the dividend to the creditors is not expected to exceed 5s. in the pound.

A great part of the losses which some of those companies have experienced has been due to the sudden winding-up, and the forced realisation of their assets. Writing more than a year and a half after the Crisis, Messrs Turquand and Harding, in their report on the affairs of Overend, Gurney, & Co., remark :—"Probably at no previous time were the difficulties in the realisation of assets and in the collection of debts so great as those experienced during the period which has elapsed since the failure of this company. The Panic which ensued was followed by depression of a universal character, and of extraordinary duration, culminating in a general absence of confidence, by which all classes have been and still are more or less influenced."

COST OF NOTE-ISSUES.

(See p. 366.)

THE expenses of the Issue Department of the Bank of England in the year 1860 are stated as follows in the Parliamentary Return dated 7th February 1861 :—

Wages,	£39,731	Stationery,	£1,811
Pensions,	8,063	General charges,	6,790
Rent,	25,600	Bank-note paper,	11,623
Repairs,	8,568	Interest on cost of machinery,	1,500
Director's allowance,	2,926	Composition paid to bankers,	20,493
Rates and Taxes,	2,300	Total,	£179,405

This sum is equal to 4-5ths of a per cent on the Bank's note-circulation, then averaging nearly 21 millions. To this has to be added the loss of interest on the gold required for the cashing of notes in the Pay Hall : but this is a trifle, certainly not exceeding £5000 a-year.

In the case of other banks, the cost of note-issues is less : for none of them find it necessary (however convenient it may be for the public) to adopt the elaborate system of registering and renewing the notes adopted by the Bank of England.

A RAILWAY RESERVE-FUND.

(See pp. 593-6.)

As we have stated in chapter XXVII., the financial circumstances of a Railway Company, at starting, closely resemble those of a Life Insurance Company. Speaking roundly, a life-insurance company starts with a stock of good lives; so that for several years it has to make very few payments for lapsed lives; and some thirty years must elapse before the deaths of its customers permanently reach the ordinary average of mortality. Hence, at the outset, such a company must set aside a large portion of its net revenue as a Reserve-fund to meet the certain increase of its liabilities. Just so is it with a Railway Company. It starts with a perfectly new stock of material: consequently for several years it enjoys a complete immunity from any costs connected with the replacement of its material. But, if it is to act fairly, and to maintain a steady and correct average dividend, the Company must put aside a portion of its profits during the first years in order to meet the heavy costs which it will soon incur in replacing its material. It is true that the traffic on a newly opened line seldom attains at once to its full proportions: and this is a consideration which may be taken into account in determining the amount to be annually set aside at the outset as a Reserve-fund. But, putting out of account this consideration—which, though important, is always of merely problematical value—let us see what is the principle upon which a Railway Reserve-fund should be established.

The various parts of a Railway have, each of them, a different period of duration. The "sleepers" last for so many years, the rails for another period, the engines and carriages for another. Each of those periods may at starting be ascertained, from the experience of other railways, with tolerable certainty; and this approximately determined longevity of the materials will regulate the amount to be annually set aside as a Reserve-fund.

Take, for example, the case of the "sleepers," which are one of the shortest-lived parts of railway-stock. Say that the average duration of "sleepers" on a line is eight years: then, an eighth part of the price of the sleepers ought to be deducted, in the early years of a railway company, from the net revenue, and set aside as a Reserve-fund to meet the replacement of those sleepers. In the first four years, there will probably be no expenditure incurred at all for this purpose; after the fourth year, replacements will begin, and they will reach their

maximum in the eighth year. From that date they will decline,—rising again to a maximum (but lower than the first one) in the sixteenth year: from which date they will again decline, and again rise to a maximum (inferior to either of the two previous ones) in the twenty-fourth year. After this time, the replacements will again sink, and remain steady at the average rate of the mortality of sleepers,—namely, the death of one sleeper out of eight every year: for by this time, owing to the renewals, the old and new sleepers (taking the line as a whole) will co-exist in nearly equal proportions,—so that, as we have said, the mortality of the sleepers will have reached its average rate. Consequently, when this period is reached, there is no longer any necessity for a Reserve-fund; and the whole liabilities of the Company in regard to replacements of this part of its material will be fairly and correctly represented by the actual cost of such replacements in each year,—which cost will form part of the annual Working-expenses.

The same principle applies to the Rails, to the Engines, and to the Carriages. It is true that, compared with the rails and sleepers, engines and carriages possess a virtual immortality. One part of them after another is replaced,—so that they still remain in working order though nearly all their parts have in succession given way, and been replaced by others. Still, a time comes when they are no longer worth mending. Even then, it is true, some of their parts may be used in the construction of the new vehicles: but, financially, this is true also in the case of rails and sleepers,—seeing that the price obtained for the old materials constitutes a deduction from the cost of the new articles.

Such a Reserve-fund would suffice to meet all replacements of material. But *additions* to the permanent way or rolling-stock must still occasion a "charging to capital." For example, say that a Company spends in one year £40,000 in adding to its carriages, with a view to obtain more traffic: say that such new traffic adds a net profit of 12½ per cent on the cost of the carriages, *i.e.* £5000; and also, that the annual appropriation of £2000 a-year to the Reserve-fund will suffice to replace the carriages when worn-out. Then—if there is to be no "charging to capital"—in the first year, the Company would pay away £40,000, and would get £5000 additional receipts, of which amount it would set apart £2000 to the Reserve-fund; so that the purchase of these carriages (though a profitable investment) would decrease the Company's dividend for that year by £37,000. Whereas in all subsequent years, the Company (after setting aside £2000 to the Reserve-fund) would have a permanent addition to their profits of £3000. Such a system will never do.

The substitution of steel rails for iron ones raises a substantially similar difficulty. In all such cases it is impossible to dispense with

the process called "charging to capital." When shareholders make an addition to their expenditure in a particular year, for the sake of reducing the working-expenses, or of adding to the receipts of the line, thereby increasing the *net* revenue of future years,—clearly, they ought not to bear the whole burden of such an expenditure: otherwise they will suffer simply in order that future shareholders may benefit. While actually increasing the value of the line, they would receive a smaller dividend than usual, while future shareholders would get a larger one. No shareholders will make an outlay upon such terms. They are a fluctuating body: and consequently it ought always to be a main object in railway finance to make the dividend of each year exactly commensurate with the value of the property. It would be unjust to the shareholders to decrease the dividend one year in order that in subsequent years other shareholders might divide larger profits.

We may add that ere long steel carriages will probably come into use,—not only as cheaper in the long run than the present carriages, but also as *lighter* in proportion to the number of passengers which they convey. Mr Wilson, the highly-accomplished Chief Engineer of the Oude and Rohilcund Company, has introduced steel carriages, and also iron-sleepers, on the Lucknow and Cawnpore line. And we believe that this system of adopting superior materials, will prove highly economical, especially in the case of Indian railways, the materials for which have almost all to be brought from this country.

THE GAS AND WATER SUPPLY OF LONDON.

(See p. 621.)

"If you want a thing done," says the proverb, "do it yourself." In regard to two most important matters it is expedient that the public of London should lay this maxim to heart. At present, as for years past, a great difficulty is felt in regard to the supply of two of the greatest necessaries of life—Light and Water. The supply of Water to London is acknowledged to be inadequate in quantity, and in most cases defective in quality; the supply of Gas is deficient in quality, and at the same time excessive in price. How are these matters to be dealt with? How are the existing evils to be remedied? The present state of matters cannot be maintained much longer. Committees have been appointed, investigations made, Parliament appealed to, and still nothing has been done. The Companies which supply the City with water and gas have a monopoly. In the case of the Gas Companies, it is illegal for any Company to start in competition with them; and as regards the supply of Water, although there is no legalised monopoly, the difficulty of finding a new source of water-supply, and the cost, as well as the vast inconvenience of breaking up the streets anew, and of laying down rival pipes alongside those of the old Companies, renders competition virtually impossible.

What, then, is to be done? On the one side stand the Municipal Boards of London, representing the three millions of the Metropolitan population, who are clamorous for more and better water, and cheaper and better gas; and in opposition to these stand the Gas and Water Companies, who naturally endeavour to turn their monopoly to the best account, by charging a maximum price while giving a minimum supply. How, then, is a solution of this most important and bitterly-contested question to be attained?

It is well to consider the case in time, lest another year be wasted and lost in the same way as this year has been. My own unhesitating opinion is, that the only way in which a satisfactory solution of the difficulty can be attained is for London to take the business into its own hands. London should be its own purveyor as regards gas and water. The supply of these commodities must always, practically, be a Monopoly; and a Monopoly, it is needless to say, is the very worst form for the public in which such operations can be conducted. The Co-operative system, on the other hand, is the best of all. Under it, there is no longer any rivalry between the producers and consumers:

for the producers and consumers are then the same persons. When a City undertakes to supply itself, there is no motive to overcharge, and the commodity is supplied at prime cost. Now, Water and Gas are of all others the commodities with which a city can most easily supply itself. The impending consolidation of the various Municipal Bodies of London into one Central Board, for the regulation of the general affairs of the Metropolis, will confer a great boon upon the community, by enabling the Central Board to carry out many beneficial changes which, with the present division of powers, is impossible. And two of the most important of those desirable changes are those which relate to the supply of Gas and the supply of Water.

As regards the Gas-question, the New System proposed in the subsequent pages was submitted to the Board of Trade, in the form of a Memorandum, on the 29th of April last,—after the Board of Trade Bill on the subject had been brought forward in Parliament. On the virtual failure of that Bill, and when the whole question was referred to a Select Committee, the Memorandum which I had submitted to the Board of Trade was published verbatim (with a few words of introduction) in the *Globe* newspaper of 13th July; and separate copies of it were sent to sixty or more Members of Parliament, including the Chairman of the Select Committee.

As will be seen, the principle of the New System was partially adopted by the Select Committee in its Report,—but in the form of a half-measure, alike cumbrous in itself and costly to the public. I hope to show, in the following pages, that the adoption in its entirety of the plan which I propose would be much more advantageous, not only from its simplicity, but also because it is more advantageous alike for the public and for the Gas Companies. It effects a reconcilement of the rival interests, upon terms permanently advantageous for both parties.

THE GAS SUPPLY.

The battle between the Gas Companies and the municipal bodies of the metropolis will soon be resumed. The next Session of Parliament will doubtless witness the final tug of war between the rival parties,—the one side striving to maintain their position of Monopoly, the other to secure for the public fair terms from the privileged Companies, or else the entire overthrow of the existing monopoly, and the substitution of a new system. It is high time that the war should be brought to a close. It has already lasted as long as the siege of Troy. It has cost £100,000 in Parliamentary expenses since 1857: and four-fifths of this sum have been paid away by the Gas Companies. In other words, the Companies have paid four times as much in the defence of their

monopoly as the municipal bodies have found it necessary to do in attacking it.

This is a curious fact. And at first sight it appears to bear heavily against the interests of the Gas Companies. It appears a great hardship that they should have to pay £80,000 in carrying on this litigation. But the case is really quite different. This large expenditure in maintaining their privileges is no loss to the Companies at all. The Companies, by the Act of 1860, are allowed to divide 10 per cent profit, but no more: and as their present profits fully amount to this maximum, the large sums which they spend in defending themselves against the public are simply a portion of their profits which they cannot appropriate to themselves, and which rightfully ought to be employed in reducing the price of gas in London. Hence the large sums spent by the Companies in Parliamentary and other litigation are just so much money taken out of the pockets of the ratepayers, and used as a means of opposing the claims and complaints of the public. Thus, so long as the present system continues, the Companies can spend any amount of money in resisting the public, at no loss to themselves,—seeing that the public have to supply every shilling of this money out of their own pockets. Thus, practically, the public have no recourse against the Gas Companies. Even when the Companies are sued and fined for supplying bad gas, or for keeping their supply to the City inadequate, and when the costs of the prosecution as well as the amount of the fine have to be borne by the Companies, this penalty is quite illusory: it is the public, after all, who have to bear the whole costs. Such a system ought certainly to be put an end to. Under it the public cannot possibly obtain redress. The Companies may spend enormous sums in defending themselves, for it costs them nothing to do so: even if they be fined enormously,—the amount of the fine also comes directly from the pockets of the community! No wonder that the Companies fight hard to maintain such a system: and no wonder that the Municipal bodies have hitherto been so little successful in their efforts to effect a change.

In fact, the power of the Gas Companies to spend money in defence of their monopoly, as well as to indulge in extravagant expenditure in other forms, is practically unlimited. Not only have they the power of so appropriating all the revenues in excess of the 10 per cent dividend (and all the Companies now pay the highest legal dividend), but they claim the right to appropriate this surplus-revenue to make up the dividends of any previous years when the dividend may have fallen below 10 per cent. In this way, they may safely spend even £100,000 in one year in Parliamentary and other expenses necessary to defend their monopoly, and yet safely rely upon every shilling of this amount being recouped to them by the surplus of future years. In other words, in

such a case, £100,000, which would otherwise go to the reduction of the price of gas, is kept from the public, and devoted to make up any deficiency in the maximum dividend of 10 per cent occasioned by past litigation on the part of the Companies.

Such a system, I say, is too monstrous to be endured. But before proceeding to detail the measure of reform which seems to me called for, it may be well to examine, firstly, the existing Act of 1860, and secondly, the plans which have been brought forward to remedy the obvious defects of that Act.

The Act of 1860.

By this Act a monopoly was conferred upon the then existing Companies, subject only to the condition that they should never pay to their shareholders more than 10 per cent for any one year. It was not contemplated that the Companies would claim the power to devote their surplus revenues in the future to make up all their back-dividends to the statutory maximum of 10 per cent. And accordingly no clause was introduced to prevent their doing so. This was a glaring oversight. And the rest of the Act was equally badly conceived. In the first place, no limit was imposed upon the charges of the Companies until their dividends reached 10 per cent ; in consequence, since 1860 the Companies' dividends have actually doubled, and in some cases trebled (in seven years !), while the price of gas to the public has not only not been reduced, but in some cases has actually increased. In the second place, when the statutory maximum of 10 per cent was reached (as it is now by all the Companies), no provision was made against wasteful expenditure and misappropriation of their funds by the Companies, so as to insure that all surplus of revenue above the 10 per cent should be devoted to a reduction in their charges upon the public. Thirdly, this arrangement gave the Companies no motive for adopting improvements in the process of manufacturing gas, nor for economising the working-expenses. Obviously, now that they have reached their statutory limit of profits, it is much easier for the Companies simply to go on as they are, and not to trouble themselves with manufacturing experiments or with the costs of their establishments ; and, under the existing Act, they have no motive whatever for attending either to the one matter or to the other. Last year, for example, one of the Companies presented their Directors—perhaps we should rather say, the Directors presented themselves—with a "testimonial" of £1500, in addition to the very handsome salary of £2500 ordinarily due to them.

The objection of the Gas Companies, that this Act of 1860 bars further legislation, on the ground of "vested rights," is wholly untenable. That Act, by giving them a monopoly (which they had not before) has been a great means of raising their profits. Without it, the

dividends of those Companies would not have risen as a whole from 6 to 10 per cent. Competition would have acted against them in a two-fold manner,—namely, by checking the extension of their business, and also by forcing them to a reduction of price in order to maintain their ground. In fact, the Act of 1860, instead of being a bar to future legislation, furnishes a greater justification for such legislation than if the Act had never been passed. It might be contended that Parliament had no right to interfere with private industry,—but this plea ceased in 1860; for the Act lifted those Companies out of the ordinary category of trading firms, and brought them thenceforth under Parliamentary supervision.

The principle of the Act of 1860,—and also of the previous Act of 1847, which was adopted as a precedent,—is fundamentally erroneous: for as soon as Companies have raised their profits to the legal maximum, 10 per cent, the Act takes away all motive for effecting any further economy. And in the case of Gas manufacture, Science is yearly enabling the Companies to produce the same results at a diminished cost.

The Bill of 1867.

Urged on by the Municipal Bodies of London, the Board of Trade this year, for the first time, consented to bring in a Government Bill to remedy the defects of the Act of 1860. This Bill preserved the monopoly of the existing Companies, but sought to regulate it in accordance with the interests of the public, by the twofold process of fixing the price of gas, and the quality of gas to be supplied at that price,—and also by altering the maximum amount of dividend to be paid by the Companies. As the dividends of the Companies, as a whole, had doubled within the previous six years of monopoly, thereby reaching the statutory maximum of 10 per cent, it was rightly concluded that the revenues of the Companies would continue to increase: and in order to give them a motive for economy, it was proposed that 7 per cent should be taken as a starting-point, and thereafter that no limit should be imposed upon the amount of their dividends.

As will be shown in the sequel, I think this method of procedure was bad in principle; nor can I say that it was rightly applied.

The Bill did not succeed. It was so strenuously opposed in Parliament by the supporters of the Gas Companies, as well as by the "joint-stock" interest generally, and found so little favour from the House at large, that it was virtually abandoned at the second reading. The main features of the Bill were left out: the price of gas was left blank, and no change was proposed in the maximum dividends allowed to the Companies. The Bill, in short, became featureless. And in this shape it was referred to a Select Committee.

Report of the Select Committee.

Although nominally the Bill was brought before the Select Committee to report upon, the measure as passed at the second reading had become a mere blank : so that nothing really was referred to the Committee but the general question between the Gas Companies and the public. As the Committee failed to come to terms with the Companies, its Report did not contain any definite settlement of the question ; nevertheless it very clearly set forth the alternative courses which, in the opinion of the Committee, ought to be adopted in dealing with the question.

The first of these alternatives thus recommended is, to proceed on the same principle as that adopted by the Board of Trade Bill—namely, to maintain the monopoly, but to regulate it in a manner conformable with the just interests of the public. The second plan (to be adopted if no satisfactory arrangement of the above kind could be made with the Companies) was to break up the monopoly of the Companies in so far as to allow of the Municipal Bodies of the Metropolis establishing gas-works of their own, and entering into competition with the Companies.

These alternative conclusions are thus expressed in the Report :—"It is our decided opinion that the consumer is entitled to a far more efficient control than he at present enjoys with respect to the supply of gas to the metropolis. . . . That it would be unjust to the consumer that he should continue subject to monopoly, and not be provided with the safeguard of effective regulation"—as to the price, quality, and quantity of the supply. "Unless the Companies are prepared during the recess to consent to a satisfactory arrangement for the consumer, your Committee think that every facility should be afforded to the local authorities of the Metropolis, in the Session of 1868, for the introduction of an independent supply. . . . The proper remedy will be for Parliament to concede to the City of London, the Metropolitan Board of Works, or other local authorities of the respective districts, the power of supplying those districts in the manner in which the corporation of Manchester supplies that city and the surrounding neighbourhood."

The First Alternative.

Of the alternative courses proposed by the Committee, the first is to recur to the principle of the Bill brought in by the Board of Trade—namely, (1) to fix the price of gas to be charged by the Companies ; and also (2) to regulate the maximum dividend which, with this fixed price of gas, the Companies are allowed to pay to their shareholders.

The object sought to be attained is, to give to the Companies an

adequate motive for further economy in the manufacture and supply of gas, by the appliance of improved processes of manufacture, which science is every year rendering available, and also by a vigilant superintendence of the costs of management; and at the same time to insure to the public a share in the results of that economy, and in the increasing profits which the Companies will make in consequence of their monopoly.

I. As to regulating the maximum dividends of the Companies.—Looking at the actual facts of the case, I do not think there can be a doubt that, if the present restriction upon the amount of the Companies' profits were removed (their present monopoly being maintained), their dividend would, on the aggregate, rise fully one per cent in the course of the following year,—owing to economies and improvements which at present they have no adequate motive to adopt. On this ground, and also *in return for a perpetuation of their monopoly*, I think 8 per cent is the highest starting-point which ought to be allowed them. Beyond that point, they should share their profits *in equal proportions with the public.* That is to say, for every one per cent of profit above 8 per cent, ½ per cent should go as a reduction in the price of gas, and ½ per cent be added to the Companies' dividends.

In this case, before their dividend again rose to 10 per cent, 1 per cent of their profits would have gone to the public in the shape of a reduction in the price of gas. Thereafter, of course, the same process would continue in force: the Companies reaping one-half of the additional profits obtained (1) by improved processes, and (2) from the natural extension of their business owing to the increase of population, and also the increase in the use of gas *per head.*

The fact that the increase of profits to the Companies depends upon these two totally different causes is, of itself, a justification for requiring that this increase shall be shared with the public. For, if the use of improved processes be due to the Companies themselves, the increase in their business, owing to the increase of population, and also to the increased extent to which gas is being used by the community per head, is due to the monopoly conferred upon those Companies, which excludes competition and places them in full possession of the field.

II. As to fixing the price of gas.—Here I must premise by a statement in regard to the practical details involved in such a mode of procedure:

The chief points in this branch of the case are (1) the Quality of the Gas; and (2) the mode in which the Price is to be determined.

The quality of the Gas depends upon its Purity and its Illuminating Power. (The quantity and pressure of the gas supplied are involved as necessary elements of the illuminating power.)

The Purity of the Gas is a matter of sanatory importance. The purity will improve in proportion to the distance from the gasometer,

—a portion of the sulphuretted elements being deposited in the pipes as the gas passes along.

The Illuminating Power, on the other hand, will be greatest close to the factory, and diminish in proportion to the distance,—the *pressure* obviously so diminishing.

In regard to the TESTING of these qualities, the object should be to apply the tests at the Main-Pipe soon after it leaves the gasometer. The ease, simplicity, and cheapness of this process, compared to testing hundreds of burners at the extremities of the system, is obvious. Of course a preliminary investigation, of a very simple kind, would be needed,—in this way. A test should be applied to the burners at the various boundaries or extremities of each system of pipes; and a simultaneous test should be applied at the Main-Pipe close to where it leaves the gasometer. And by comparing the pressure and illuminating power, &c., of the Gas at the Main with the results simultaneously given at the extremities, it could thereafter be ascertained, by simply testing at the Main, whether or not the supply was adequate at the extremities. Of course, as the use of gas is yearly increasing, these simultaneous tests at the Main and at the extremities would require to be repeated at distant intervals: but the testing at the Main would be sufficient in ordinary circumstances.

It seems to me a mistake to make the price charged by the Companies vary with the quality and quantity of the gas supplied. These may vary from week to week, and ceaseless difficulties would arise in connection with them. It would be much better to require that all the Companies shall at all times furnish gas of a certain purity and illuminating power. And let a *heavy* fine be imposed upon every breach of this condition.

In fact, the Gas Companies should be dealt with somewhat in the same way as Distillers are. Let officers (like those of the Excise) be appointed under the Act to test the gas, not at certain times, but whenever they please. Let those officers have a fair salary, and give them a large share in the fines imposed on the Companies. The Companies could protect themselves as distillers do, by seeing that the facts are truly stated by the officers,—for, with good tests, the strength and quality of Gas can be determined as easily as the alcoholic strength of Spirits.

If this plan were adopted—that is to say, if the Companies were bound at all times to supply gas of a fixed purity and illuminating power—one element of perplexity would be removed; and the difficulties of prosecuting the Companies and getting a verdict (at present insuperable) would be greatly lessened.

But there are great difficulties in the way of attaining a satisfactory settlement of the question in this form. A Select Committee of Parliament is doubtless the only proper tribunal for fixing the two start-

ing points,—namely, the Price of gas and the maximum Dividend which, with this rate of charge, the Companies shall be allowed to appropriate. But, after the experience of the present Session, it appears hopeless to expect that any agreement can be come to with the Companies upon these points, unless by sacrificing the interests of the public. Moreover, I do not believe that any Committee can, with confidence, decide upon these points,—and most of all, as to what is a fair price for the supply of gas of a certain fixed quality.

The Second Alternative.

The Committee themselves evidently regard the adoption of their first alternative as almost hopeless; and I think it a bad one. Let us now consider the other alternative,—namely, that the Monopoly of the Companies should be abolished, so as to allow the Municipal bodies to erect gas-works of their own, and to enter into competition with the Companies.

Now, there can be no doubt that, under such a system of competition, the Municipal bodies would quickly drive the Companies to the wall. Instead of their present affluent condition, the Companies would see their dividends rapidly decline. They would have to reduce their charges: yet even with this change they would not be able to hold their ground. The Municipal bodies are, in fact, the Public. The work which they undertook would be undertaken simply in the interests of the public. Moreover, their costs would have to be supplied by the public. So that the public, for their own interest, would support the Municipal gas-companies, and abandon the existing Companies. In this way, I repeat, the Companies would soon be driven to the wall.

But, consider the immediate disadvantages and inconveniences of such a system. For some years, these Municipal gas-works would not pay the very heavy expenses requisite for their first establishment. Although these Municipal Companies (so to call them) would be sure of success in the end, they would, at the outset, be subject to all the serious drawbacks which would attend new private Companies. As the Select Committee themselves remark:—"The difficulty of finding room for mains and service-pipes in the already crowded line of the streets, the public inconvenience of frequently disturbing the pavement, the objections usually entertained by the inhabitants of populous districts to the introduction of new gas-works, &c.; all are obstacles, in addition to those which are connected with the raising of the capital required for so great an undertaking as that of supplying with gas any large portion of the metropolis."

A New Plan.

The proposal of the Select Committee is in the right direction. But it is a half-measure, and is accompanied by great disadvantages which

would disappear if the principle were at once carried out to its legitimate issue.

The result of the plan proposed by the Committee would be so to reduce the profits of the existing Companies as to make these Companies willing to retire altogether from the field, and sell their gas-works and pipes to the Municipal Companies. Now, it seems to me that this result could be better accomplished at once, than by adopting a system of competition onerous to the Municipality, and also detrimental to the Companies. As regards the existing Companies, they could not expect to obtain such good terms for transferring their works and business *after* their dividends had been reduced by competition, as they fairly can at present, when their dividends are at their highest point. Why, then, should not the Companies be ready to make the transfer of their business to the City *now*, when their profits are at the highest point they can possibly reach, than wait until their profits are reduced by the competition of the Municipal bodies, and when of course they will not get as good terms as would be offered them now?

This is the solution of the question which I propose. And it seems to me unquestionably by far the best arrangement which can be made, as regards the interests alike of the Companies and of the public.

The supply of Gas is a business which every township or Municipality should, and can advantageously, take into its own hands. When left to a private Company, this business always occasions endless strife and dissatisfaction in the community; and also some cost and much inconvenience by the breaking-up of the causeways, &c. Moreover the supply of Gas, as of Water, is a kind of business more suitable than any other for the management of a Municipality. As soon as the primary works are completed, the management is very easy and simple. Any kind of business (from Banking down to shopkeeping) which requires a daily superintendence—where the conditions of the business fluctuate from day to day, or even from week to week, is not suitable to public bodies, and ought to be left to private management,—both on account of the close attention which such business requires, and also owing to the *risks* which attend it. But the case is different with the supply of gas, where there are no fluctuations, and where the only change which takes place is a gradual increase in the demand for the commodity supplied.

In determining what would be a just price to be paid to the Gas Companies, the Select Committee should take into account not only the fact that these Companies owe their present profits, in some degree, to the legislative monopoly conferred upon them in 1860, but also that the continuance of their present rate of profit is to some extent dependent upon the maintenance of that monopoly. If Parliament were to annul that monopoly, it is at least possible that the fervour of competition (as soon as speculation recovers from its present abnormal

state of depression) would suffice to force the existing Companies to reduce their rates simply in order to deter contemplated new Companies, or to drive them out of the field if they were established.

But, in truth, such considerations need not be entered into. The only fact to be noted is, that all the Companies now pay a dividend of 10 per cent, and that this is the highest rate of profit allowed by the Act, and which they can possibly claim.

Financially, this transfer of the property of the Gas Companies to the Municipal bodies of London could be easily effected. When a new road is wanted in any district, a Corporation borrows money, and pays the interest on the loan out of the proceeds of the tolls,—any deficiency, of course, being supplied by an increase of the local rates. But if the London Municipality (so to call it) were to buy up the rights and property of the Gas Companies, no new rate would be needed at all. Even from the outset, no new charge would be imposed upon the public; while there would be a yearly increasing gain from the reduction of the existing charge—namely, the price of gas.

The transfer of the property of the Gas Companies to the Municipality (so to call it, or the aggregate municipal bodies) can be effected without any *direct purchase*, and *without any loan or other financial process*, on the part of the Municipality. All that is required is to convert the Shares of those Companies into City Bonds of equal amount, bearing 10 per cent of yearly interest. The funds necessary for the payment of interest on these bonds are already in existence: they are supplied by the proceeds of the rate at present levied upon the community by the Companies. The only change which would be made would be that the present amount of the Gas-rate would be collected by the Municipality, and paid to the shareholders of the Companies as interest on the Bonds, instead of being collected by the Companies themselves, and paid by them as dividend to their shareholders.

This is all that is necessary in order, by one stroke, to transfer the property and interests of the Gas Companies to the Municipality. *No loan or new rate would be needed at all.* And no loss could possibly happen to the Municipality from the arrangement, seeing that the funds required for the annual payment on these new City Bonds are already in existence.

Advantages of the New System.

The advantages of the New System to the community would be twofold,—alike economical and (what for want of a better word we must call) Social. There would be not only the acquisition by the public of the prospective profits on the supply of gas, but also an immediate advantage by the more economical management of the business; and likewise there would be a greater satisfaction on the part of the public, seeing that they would no longer have to deal with private Companies, inclined to extortion, but would actually have the management in their

own hands. Instead of the existing conflict between the interests of the Public and of the Traders, we should have a Co-operative System under which this antagonism of interests would disappear. The community would be alike the producers and the consumers.

But in estimating the working of the New System, let us look a little more into details. The points to be noted are—(1) The Collection of the Gas-rate : (2) The Management of the Business ; and (3) The Prospective Profits.

(1) The Collection of the Rate would be made by the Municipal Bodies ; and as there is already a Municipal Staff for the collection of rates, it is reasonable to infer that the collection would be made more economically than by the existing companies, each of which has to maintain a staff of collectors for this purpose alone.

(2) The Management would doubtless be intrusted to a Commission, appointed by the Municipal bodies, the members of which would be removable, or subject to re-election, every 3 or 5 years. But probably it would be better (especially as the system is the result of Parliamentary legislation) that a portion of this Commission, say one-fourth, should be appointed by the Board of Trade ; and probably, also, it would be better, in the interests of the community, that these should be permanent members—like the permanent secretaries in the various Government Departments—who would thereby acquire a more complete knowledge of the business than the temporary members who would represent the fluctuating views and interests of the public.

As this Board, or Commission, would take the place of ten different Boards of Directors, each with its Accountant, Secretary, &c., it is reasonable to infer that the members of it might be paid a salary sufficient to secure their whole time and ability,—and yet the cost be considerably less than that incurred for the same purpose by the ten Companies now in existence.

Thus, upon both of these heads—the Collection and the Management—there would certainly be a considerable gain ; besides the greater satisfaction to the public, *i.e.*, the payers of the rate.

(3) As to Prospective Profits.—The fact that the dividends or profits of the existing Companies have almost doubled during the last six years, is, of itself, a sufficient proof of the great increase of profits which may be reckoned upon in the future. An addition to the existing rate of profit may be safely reckoned upon from three different causes. (1) The increased use of gas, in lieu of lamps or candles, even if the population remained stationary in numbers and wealth. (2) But the population is increasing alike in wealth and in numbers, so that a great additional profit may be expected from this cause. (3) The adoption of improved processes in the manufacture of gas. Under this head a considerable prospective gain may be confidently relied on. For

example, in the analogous case of locomotion, Science has produced so great an economy that the same amount of coal can now be made to produce a double amount of steam-power compared with the state of matters 20 years ago. In like manner it may be expected that, by improved processes, the same quantity of coal will ere long be made to produce a greater quantity of gas; and also, that inferior kinds of coal will be made to produce gas of an illuminating power equal to that produced at present by more expensive kinds.

The additional profits, or increased economy, arising from these various causes, would go entirely to the benefit of the public, in the form of a reduction of the price of gas. So that, as the result of the New System, London would soon be supplied with gas of a superior kind at a constantly decreasing price. At the same time the present strife and dissatisfaction would disappear, as the community would then have the business in its own hands; it would be at once Producer and Consumer—and would no longer have to struggle against the interests of an alien (*i.e.*, private) body.

I may add, in conclusion, that there is no need in this case to establish a Sinking-fund for paying off the bonds. There is no loan to be extinguished: there is no *new* rate to be gradually got quit of. If the shareholders of the Companies get 10 per cent on their capital, that is all that they can claim: it is also all that they can desire. The Bonds themselves would be convertible into the capital, by sale on the Stock Exchange. Neither would there be any advantage to the community in paying off these Bonds by a Sinking-fund. For the only result of a Sinking-fund would be, that a portion of the yearly profits would be set apart for this Sinking-fund, instead of being applied to a reduction in the price of gas. So that, in fact, to establish a Sinking-fund in any form (*i.e.*, either by converting the Bonds into terminable annuities, or otherwise), would be simply to make the present householders of London *pay* for giving cheaper gas to other householders who may succeed them, and with whose interests they are in no way connected.

THE WATER SUPPLY.

Three conditions are requisite to constitute an efficient system of Water-supply. First, the quality of the water must be above suspicion, and such as is consistent with perfect health on the part of those who use it. Secondly, the quantity of the supply must be adequate for all the personal, domestic, and civic purposes for which it is required. Thirdly, the supply should be constant, so that it may be available whenever it is wanted.

It is needless to say that the existing water-supply of London is

inadequate in each and all of these respects. It is needless to recapitulate the experiments of Dr Letheby, nor the investigations of Captain Tyler and others, nor the never-ending civic complaints upon the subject. But I may say a word as to the great advantage, if not necessity, for the establishment of a system of "constant supply"—a point to which too little attention has yet been given:—

It is only when in some emergency an urgent demand for water is unsatisfied that people are aroused to the conviction that the system of supply is inefficient. A great fire rages at night and there is no water wherewith to extinguish it; the drains are at fault in a hot and dry season, and there is no water with which to flush and cleanse them; or the arrangements of the Water Companies clash with certain domestic customs. In all of these cases there is an outcry; but, except at such junctures, people generally are unconcerned, and suffer very placidly a number of evils of which, indeed, they are probably more or less unconscious. It is not, however, only on occasions such as those to which reference has been made, that the public is injured by the insufficiency of a system of supply which is not always available. A great evil results from the fact, that when the supply is not constant the water must be *stored* for use. Water which has lain long in a cistern exposed to air can, at best, be only tolerably free from impurity: and in many cases, especially in poor localities, from the difficulties incident to the cleaning of the cisterns, the water becomes unfit for use. In short, in the case of a vast population, like that of London, it may be unhesitatingly affirmed that no supply can be perfect which necessitates storing. These and other matters require only to be investigated in order to prove that it is indispensable the supply should be available at all times and under all circumstances when it may be needed.

It has been abundantly proved that water at full pressure ought to be available for the wants of the community at all times. Why do we hear of difficulties? Is it not absurd to talk as if a system which is adopted in the provinces were impossible in London? The objections which have been raised to the system of constant supply are perfectly inexplicable. The very means which are in use in some of the provincial towns have been declared impracticable, and contingencies which never occur have been represented as inevitable and inseparable. Bursting pipes, leaking taps, wanton waste, and a host of similar bugbears, have been pictured *in terrorem* of a constant supply, until it has come to be regarded as at least doubtful, whereas at the same instant the system is in full work out of the metropolis.

No doubt, if the present system is maintained, there are great, indeed insuperable, difficulties in obtaining for our vast metropolis an adequate supply of water. Not only is it difficult to insure a supply of pure water, but the quantity of the supply, at present inadequate, must yearly

become less adequate, owing to the growth of the metropolis. More water is needed if any great improvement is to be made in our sanitary arrangements, and in the habits of the lower classes; and more water is also being consumed by the yearly increasing use of steam-machinery.

It may not be easy to say whence this new supply of water is to be obtained, but it is certain that the process of obtaining it will be exceedingly costly. The project of bringing water from the Cumberland Lakes, by a grand aqueduct running right across England, is chimerical; for this reason, among others, that it would be resolutely opposed by Liverpool, Leeds, and all the towns of the North, who would assert a prior claim to the water of the Lakes. A more feasible plan would be to establish reservoirs in some of the narrow upland valleys of Wales, and bring the water to London by great aqueducts. Nevertheless, the first point that is incumbent is, that we should fully utilise the rainfall of our own district of the London basin, — the valley of the Thames extending up to Oxford. Parliament may give great help in this matter by rendering compulsory the utilisation of sewage, or at least of preventing the sewage of towns being simply poured into our rivers. But it will take some time before so great (and beneficial) a reform can be effected. Until this change be effected, it seems to be almost imperative that the reservoirs for the supply of London, instead of being kept close to the metropolis, should be constructed on the upper course of the streams—there collecting the flood-waters, and at the same time escaping the impurities of the streams in the lower part of their courses. But one important point to be attended to is this,—the surface-water of the London basin by no means represents the entire rainfall of the district; perhaps an equally large portion finds its way through the surface-soil, percolating down through the surface-soil, and forming a vast source of subterranean water-supply. Doubtless a portion of this subterranean water finds its way to the surface again in the form of springs; and we are very sure that this source of water-supply has not yet been sufficiently attended to. But a still more important means of adding to our supply of water is by the sinking of Artesian wells—by perforating the strata until some deep subterranean reservoirs are reached, from whence their pure waters might be brought to the surface. We have little doubt that Artesian wells will be adopted as one of the means of improving and increasing the water-supply of London. The other method is the establishment of large reservoirs at a distance from London, and conveying the water to the metropolis by costly aqueducts.

But we repeat, whatever be the processes adopted for obtaining a better water-supply for London, those processes will be very costly. As a natural, indeed necessary consequence, the existing Water Companies will be most reluctant to undertake so serious an enterprise.

We do not believe that any of the present Companies would consent to so widely extend their capital and their operations. Still less is it to be thought that any new company would be willing to engage in so costly an undertaking, when the prospect of adequate remuneration amid the competition of the established companies is absolutely hopeless. The work, we believe, could only be accomplished by means of a guarantee from the Municipality of a certain profit to the Companies (say five per cent) upon the capital which they embarked in such undertakings. And, when it comes to this, it were better for the Municipality to take the work into its own hands.

There are many other reasons why the Municipality should take this course. Indeed, all the arguments which I have adduced in favour of the Municipality taking into its own hands the supply of Gas, are at least equally applicable to the supply of Water. The whole facts of the case concur in demonstrating the advantage of taking the supply of water out of the hands of the Companies (of course, with adequate compensation to these bodies) and combining the works and administration of the eight existing Companies under a single Board appointed by the Municipality. The population of London is a nation of itself: and it ought certainly, alike on economical and on social grounds, to abolish the present inadequate system of water-supply by means of private companies, and establish a new and better one in which the Municipality itself will be the manager, and the public will be at once consumers and producers.

The financial process by which the property of the Water Companies can be transferred to the Municipality is identical in principle with that which I have fully detailed in regard to the question with the Gas Companies. The only difference is, that (1) the Water Companies possess no legal monopoly; and (2) that their dividends, as a whole, have not (like those of the Gas Companies) reached the maximum allowed to them by Act of Parliament.

In conclusion, it seems to me that the sooner these questions, embarrassing though they be, are grappled with the better. An efficient water-supply especially, is of the very highest importance to the welfare and health of the metropolis: it is a want far more urgent than that for a Palace of Justice, or for a new National Gallery.

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WORKS BY R. H. PATTERSON.

THE NEW REVOLUTION;

OR, THE

NAPOLEONIC POLICY IN EUROPE.

(1860.)

British Quarterly Review.

The author of this book holds rather an enviable position. He has prophesied—and he has lived to witness the fulfilment of his prophetic visions. To the mind ignorant of the deductive value of history, his book would be doubtless suggestive of Zadkiel himself. But Mr Patterson's philosophy is based neither on the language of the planets, nor on the mysterious figures of the Apocalypse, but simply on the logic of facts. . . . Such a small compass of history as the present generation has lived has rarely been pregnant with so much logic.

Revue des Deux Mondes.

Les articles de M. Patterson, reimprimés depuis en volume sous le titre de *la Nouvelle Révolution*, lui aient valu la reputation de prophète, et d'ingenieux penseur politique.

The Dial.

This book is a study in the history of the present time. The Emperor Napoleon, his character, his career, his policy, his imperial system, his place among European potentates, and the scope of his designs as affecting the state and prospects of European nations—such is the theme of Mr Patterson's book. . . . The book is, in all respects, able. . . . We have confidence in pronouncing these articles among the ablest contributions ever made to journalism, and in saying that Mr Patterson would be a distinguished historian if he were not the distinguished editor of a Tory newspaper. His style is clear, nervous, and dignified, admirably adapted to the treatment of a grave historical subject, and rising at times into noble though chastened eloquence.

Illustrated London News.

The remarkable feature of the papers of which the volume consists is, that most of them were written at a time when the circumstances which they dwelt on were either unthought of or disregarded; and therefore subsequent events have given to them a character of prescience which rises almost to the height of prophecy.

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If Mr Patterson's merits as a political writer be judged of by the truthfulness of his speculations, he will be found to have scarcely a compeer. In his articles in 'Blackwood's Magazine,' almost every step that Napoleon has taken was predicted, and almost every political event forestalled. . . . The profound observations which this book contains, and the vigorous idiomatic style in which they are expressed, will interest the reader.

Bell's Weekly Messenger.

Whatever may be the eventual consequences to Europe of the modern Napoleonic policy, it can never be said that there are not some far-seeing men on this side of the Channel who have not, from the very first moment of the Imperial career, marked its tendencies, and given warning of the natural results to be anticipated from its extraordinary manœuvres. In all our experience we do not think we have met with one of these who has so thoroughly accomplished that purpose as Mr Patterson, the author of the book before us. . . . At the close of 1856, Mr Patterson thus wrote of the prospects of peace, and of the causes which must eventually induce war, the force of which has now the reality of a fulfilled prediction:— . . . This very important book ought to commend itself at once to every Englishman, and obtain hosts of readers.

The British Controversialist.

A masterly exposition of the designs and tactics of Napoleon III. It is full of cogent reasoning, singularly lucid explanations of the means, purposes, and results of the imperial manœuvres, and almost prophetic deductions from the past facts regarding future exigencies. The style is vigorous and idiomatic; and the far-seeing sagacity and sleuth-hound-like pertinacity of logic in tracking the political purposes of the Ulysses of the Tuileries, supplies it with nerve, eloquence, and invective, as well as argument.

Edinburgh Courant.

A volume, which we may truly call remarkable, has just been published by the Messrs Blackwood. It contains a masterly exposition of the designs and tactics of the Emperor of France. . . . A writer who shows himself so thoroughly well acquainted with the subject he undertakes, as to be able to anticipate the course of events with such remarkable exactness, is entitled to be listened to with profound attention. He can have no interest or object but truth. Party zeal will pervert a man's judgment, not strengthen and improve it; but the judgment which shows itself to be so clear and correct in its inferences must move in a sphere far removed from the distorting medium of mere Party. It is for this reason that we would invite attention to the remarkable exposition of the policy and plans of Napoleon as here unfolded.

The Economist.

"The New Revolution" proceeds from a pen to which one of our weekly contemporaries has of late been deeply indebted. . . . Mr Patterson differs in one important qualification of a public writer from the

majority of those attached to the Conservative party. They are too generally neglectful of facts, somewhat careless of principle, and prone to personality. In the present *brochure* we are glad to notice that the writer's evident party-bias never leads him astray in this direction; and that even Mr Bright is mentioned in a manner corresponding with the dignity of the critic.

Morning Advertiser.

Should any ardent Liberal take up this volume, making up his mind that, however cordially he may admire its ability, he must necessarily disagree with the author's sentiments, and with his view of men and measures he will enjoy a very agreeable disappointment. . . . It would be well for the country if such a volume as this, in some cheap and popular form, could be scattered broadcast throughout the length and breadth of the land, perused and pondered by every thinking man in the entire community. . . . The author is entitled to take his place in the foremost rank of the patriotic politicians of the present day.

Morning Herald.

To write contemporary history is proverbially an insurmountable difficulty. But the author of the present volume has been enabled to write a passage of contemporary history with a general correctness of outline, and a broad truth of interpretation, which there can be little doubt will stand the test of future criticism, when time shall have placed the world upon a vantage-ground from which to look back upon the Past as on a vast plain extended at its feet and visible in every detail. . . . Although the general tone which pervades the book is eminently calm and philosophically argumentative, the author at times rises to an unusual degree of warmth and emphasis, and becomes nervous and eloquent.

St James's Chronicle.

A very remarkable volume. . . . It is a graphic and almost prophetic sketch of the policy and principles of Louis Napoleon. . . . We do most earnestly beg of our readers to study Mr Patterson's work. It is thoughtful, dispassionate, and statesmanlike.

Literary Gazette.

The style is as vigorous as we have ever met with, and the invective is of the most powerful kind. We strongly recommend the book to the attention of our readers.

Leader.

Mr Patterson is right in looking upon Europe as upon the verge of a new revolution—a great change in boundaries, governments, and ideas. Mr Patterson well remarks:—"The rights of man, as understood by the Convention, was the idea developed by the first Revolution: the rights of nations, as interpreted by Louis Napoleon, is the corollary idea which the new Revolution proposes to realise." Such a policy, if unchecked by sudden accident or wise counteraction, must, as Mr Patterson supposes, end in a Great War, in which it is difficult to imagine that we can escape.

ESSAYS IN HISTORY AND ART.

(1862.)

CONTENTS.

COLOUR IN NATURE AND ART.
REAL AND IDEAL BEAUTY.
SCULPTURE.
ETHNOLOGY OF EUROPE.
UTOPIAS.
OUR INDIAN EMPIRE.
THE NATIONAL LIFE OF CHINA.
AN IDEAL ART-CONGRESS.
BATTLE OF THE STYLES.
GENIUS AND LIBERTY.
YOUTH AND SUMMER.
RECORDS OF THE PAST: NINEVEH AND BABYLON.
INDIA: ITS CASTES AND CREEDS.
"CHRISTOPHER NORTH"—IN MEMORIAM.

Dublin University Magazine.

Not often, whether in prose or verse, does the same man command both "the vision, and the faculty, divine." Not often is the original thinker endowed with a fluent and fascinating style, which takes captive the crowd by its beauty. Mr Patterson has this good fortune. He is an unquestionably original thinker, whom some readers might deem too daring; and he has a noble and eloquent style, which also some might consider too ornate. He is a writer so full of novel and unusual thoughts that he throws them into notes, and encloses them in parentheses. His writing is pictorial, and very full of colour, yet it never lacks precision. . . . We have hitherto made reference only to Mr Patterson's most thoughtful and philosophical essays. But the volume is diversified with "light reading." "Genius and Liberty" is a delightful essay, full of poetic ardour. "Youth and Summer" is nothing less than a prose-poem—and that of no common kind. In "The Battle of the Styles" is condensed an immense amount of wit and wisdom. Mr Ruskin's delightful fallacies are treated with admirable humour; and the despot of art is as pleasantly bantered by his reviewer as was Robert Montgomery by Macaulay. . . . We can sincerely congratulate Mr Patterson on having by this volume shown himself as original a thinker on subjects of general History and Art as he had previously proved himself to be on the contemporary history which we call Politics. He has insight, logic, humour, a noble and variable style, and can claim entrance by right to the first rank of authors of the day.

Athenæum.

In Mr Patterson's Essays we have a volume which no discerning reader will open only once. Fine appreciative taste and original observation are found united with range of thought and rare command over the powers of the English language. . . . Our judgment leads us to prefer his Historic dissertations. And the treatise we should adduce before all the rest in support of the high opinion we entertain of the author's powers is that on "The National Life of China." For breadth and strength of handling, completeness of grasp, judicious arrangement of material, and lucid style, it is a model of what such a performance ought to be. . . . It is impossible to convey in a brief space any adequate impression of a collection of papers written on a variety of subjects, and holding in every page proofs of unusual research and capacity. To form a fair opinion of Mr Patterson's merits, readers must get his volume.

Macphail's Edinburgh Magazine.

A philosopher asserts that Genius is the power of attention, producing Originality. If this be so, no one can have a fairer claim to its possession than Mr Patterson, since all his writings are marked by a most striking originality, in thought and in expression. . . . Mr Patterson's present work is executed with great literary ability. The style is terse, vigorous, chaste, pictorial, and lively. Thoughts, original and suggestive, startle us in almost every page; and the matter is of the most solid kind,—presenting a striking contrast to the superficiality which characterises so many volumes of a similar description.

Revue des Deux Mondes.

C'est un plaisir assez singulier que nous a procuré la lecture des *Essais* reunis de M. Patterson. . . . M. Patterson est sans doute un homme supérieur; et il est loin de laisser faire ces instincts qui sont entrés en lui par droit de naissance—ces génies de son temperament: toujours est-il qu'ils sont bien en lui. Quoiqu'il ait aussi son côté poétique, c'est un esprit essentiellement clair et logique,—qui aime à spéculer, à embrasser des vastes ensembles, et qui procède volontiers par des séries consécutives de raisonnements,—un esprit chez qui le besoin de comprendre, d'expliquer, et de résumer l'emporte d'une manière decidée sur le sentiment et sur les émotions capricieuses de l'imagination. . . . On ne s'étonne pas que ses articles sur la politique Napoléonienne (articles réimprimés depuis en volume sous le titre de *la Nouvelle Révolution*) lui aient valu la réputation de prophète et d'ingenieux penseur politique. S'il aime à généraliser, c'est en homme qui voit vraiment toutes les grandes données d'une question. . . . Dans ses instincts, comme dans son intelligence, il n'a rien d'exclusif. Cette disposition à rendre égale justice à tous le sert bien dans ses appréciations. . . . Une des qualités qui ont le plus contribué à sa supériorité c'est qu'il est viril. Il a le sentiment de la Réalité,—il ose la régarder en face: et cela n'est pas un mince avantage pour éviter toutes les extravagances qui aujourd'hui s'appuient sur tant de naïve sentimentalité.

L'Independance Belge.

La lecture de ce livre atteste à chaque page que l'auteur traite de la peinture avec le pinceau d'Apelle, de la sculpture avec la ciseau de Phidias, de l'architecture avec le compas d'Ictinus. . . . La nouveauté des aperçus étonne tout d'abord le lecteur, qui se prend à accuser l'auteur de métaphysique ; mais bientôt il est forcé de revenir sur cette première impression devant la preuve mathématique. . . . Quant au style, il est toujours clair, mais toujours éloquent,—toujours simple et toujours attrayant. Enfin, c'est un de ces ouvrages qu'on ne lit pas à moitié, mais jusqu'au bout, et qu'on retrouve toujours avec plaisir.

The British Controversialist.

In all of these Essays there may be found able writing and profitable reading—profound thought, and the issues of a mind of singularly prolific suggestiveness and breadth of culture—of a nature of excellent original material, well cultured and trained. . . . The essays on "Our Indian Empire" and "India : its Castes and Creeds," contain an extraordinary amount of historical information, philosophical speculation, political discussion, moral hints, and religious suggestions, evidently at once the results of wide study and of profound thought. . . . The essay on China enters more completely into the state of thought, feeling, being, culture, and the influences of politics on these, than any book we have ever read on the Melchisedec of nations.

Morning Herald.

A volume of essays of this kind is as rare as it is acceptable : rare, because few men really qualified to deal with such subjects from practical knowledge can write with such power and elegance as Mr Patterson ; and acceptable, because modern essays are, for the most part, mere light exhibitions of gossip for readers of magazines. The papers in this volume are very various, both in choice of subject and in style of treatment ; but in them all are to be found traces of research and of careful thought, combined with great freshness and originality in conveying information. . . . These Essays are worthy of the most careful study, not only of the general reader, but of the Scholar and the Statesman. They are learned without being pedantic ; amusing without being trivial ; and marked throughout by purity and strength of thought and language.

Morning Advertiser.

Fully understanding and appreciating the refined and humanising pleasures of taste, Mr Patterson revels in a style copious and beautiful, replete with harmony and grace—at times simple yet poetic, never affected, and, when figurative, free from all exaggerated amplification. . . . The reader, led away by magnificent descriptions of the blue above and the green below—sapphire and emerald—imagines he is looking at those grand pictures by Turner (now growing mellow, and fast, we hope, eclipsing Claude's) : while he is only perusing Mr Patterson's pages about the gorgeous sunset—clouds and sky filled with richest colouring—brilliant ever-shifting hues which at once dazzle and mock.

We are gratified that we have a writer—our author—able to wield a pen with as much effect as the clever writer of "The Stones of Venice." Mr Patterson's work does honour to the literature and art of our common country.

The Globe.

The tone of thought and feeling in these Essays is so thoroughly elevated above commonplace, that they deserve attention from all with whom the banishment of commonplace in literature is a thing aimed at or longed for. . . . One of the best of these Essays is on "Real and Ideal Beauty." Mr Patterson has a fine feeling for true art, and propounds the theory of man's desire for Perfection as the cause of his love of the Beautiful. He is opposed to the Alison and Jeffrey "association theory," and has much to say on the subject of the Science of Proportion, and on the value of scientific method in Art-studies. . . . Mr Patterson's mind is not merely artistic. One of the best papers is on the Ethnology of Europe. The account of the successive waves of races from the East, sweeping over Europe with more or less rapidity and completeness, is better than most similar accounts with which we are acquainted. It is concise, clear, and well illustrated.

Literary Budget.

Writing which merely amuses is in these days so plentiful, that it is quite refreshing to meet with writing which suggests. Mr Patterson is a remarkably suggestive writer—a theorist of no common order. . . . There are many parts of this thoughtful and suggestive book which we regret to leave unnoticed. It is a volume which any one who has a week's holiday should put in his knapsack, so that he may have fresh and startling thoughts while he sojourns amid the solitary mountains or beside the mystic sea.

The Dial.

Mr Patterson's Essays will bear comparison in almost every respect with the best compositions of the kind. They exhibit a sustained power and brilliancy which are highly uncommon; and for closely-packed information, and steady flow of ingenious and pleasing thought, we know not where to find them surpassed. While sparing himself no labour, Mr Patterson exerts his utmost skill to save labour to the reader. His writing is perfectly lucid, and is accompanied by a glow of imaginative fire. One talent exhibited in rare perfection by Mr Patterson is this, that he can visit other lands in the pages of travellers' books, and give such vivid descriptions of what he has found within the boards that you feel certain he paints from sight. He depicts scenes of another hemisphere to the life. . . . Such is our honest opinion of this able and eloquent book. It is at once a magazine of information and a gymnasium for thought.

Saturday Review.

Mr Patterson is a really cultivated and accomplished man, who has read and thought much on the subjects about which he writes. . . . We have said enough to show that the present volume will repay perusal.

Illustrated London News.

These Essays are from the pen of the author of a very remarkable work, entitled "The New Revolution; or, the Napoleonic Policy in Europe," which attracted attention soon after its publication, owing to the singular fulfilment of certain predictions which it contained. The present work is altogether of a different mould, and ranges through such a series of subjects that one rather wonders at meeting with a man so various as the author. There are about the Essays all the marks not only of a thorough acquaintance with their respective subjects, but a spirit and a tone which show that the author is writing from his own inspirations.

Art Journal.

These Essays ought to take a place by themselves in the library. There is not one of them which will not amply repay the reader. They deserve to be classed among the best writings of the kind to be found in the literature of our day. They are eminently practical; while the views and doctrines propounded are set forth in language terse, simple, and elegant. Mr Patterson argues forcibly, yet in a catholic and gentle spirit. No knight who tempts his lance need fear unknightly conduct in a tournament of letters.

Revue Contemporaine.

Un vif sentiment de la beauté—un langage animé, coloré, parfois lyrique—des aperçus souvent ingénieux, prêtent un charme réel à ces esquisses. La valeur principale du livre de M. Patterson, cependant, nous semble être dans sa partie plus *positive*,—dans les *Essays* si étudiés et si élégamment écrits sur l'ethnographie de l'Europe, sur la vie nationale en Chine, et particulièrement dans deux études sur l'Inde, qui prennent presque la moitié du livre. On y reconnaît à chaque page la féconde alliance de l'écrivain érudit et de l'homme d'Etat.

L'Avenir Commercial.

La meilleure preuve que M. Patterson a été bien inspiré en publiant ces *Essais*, c'est qu'il nous a intéressés à des travaux très variés. C'est en écrivant d'une manière atachante que l'auteur nous conduit de l'Europe aux Indes, des bords du Gange en Chine, de l'empire du Milieu à l'île d'Utopie,—ou qu'il nous fait remonter aux temps où florissait Ninive la puissante et Babylone la grande,—qu'il nous fait assister ensuite aux joûtes oratoires de Grèce, ou à un congrés imaginaire, mais moderne, des Arts. . . . Disons en passant aux économistes et aux statisticiens, que les chiffres ne manquent pas absolument dans les articles de M. Patterson, mais ils sont si bien amensé, et employés avec tant de discernement et de sobrieté, qu'on ne s'en aperçoit guère.

Kolnische Zeitung.

In the midst of the immense mass of works published on History and Art, Mr Patterson's book is a refreshing oasis for the mind. These Essays are distinguished alike by their profound learning and by the originality of their contents. . . . A work of genius—of eminent value.

China Mail (Hong-Kong).

Mr Patterson's Essay on "The National Life of China" is by far the best *résumé* and bird's-eye view of the history of China that we have yet come across. Indeed there is nothing of the kind elsewhere with which it can be compared; and we cordially commend it to all those who really desire to make themselves acquainted with the history of China and the character of its national life.

Dublin Warder.

These Essays are the production of a happily-constituted intellect—far-seeing, comprehensive, unprejudiced, lucid, many-sided, richly informed. . . While the book is sure to be welcomed by the Artist and the Philosopher, it cannot fail to be acceptable to every class of intelligent readers, owing both to the interesting nature of the topics, and to the clear and finished style in which the information is conveyed. We have had such refined and elevated pleasure in reading these Essays as does not often fall to the lot of the critic. . . . Mr Patterson is a man of rare powers of mind, and his work is well worthy of an honoured place among the choicest volumes in the library of persons of taste and erudition.

Liverpool Albion.

The subjects treated of are varied, and all interesting in themselves, while they claim a wide extent of general attention from the felicitous mode in which they are regarded and displayed by the author. . . . In the first three Essays, which are so kindred in relation as to form almost a unity in design, there is manifested a fine play of speculative philosophy, which, without fettering by dogmatic rules, leads directly to practical results. The author of these Essays is obviously well skilled in those peculiar elements of thought which enable a man to take a comprehensive view of artistic composition. Shakespeare says of Cassius, with telling aptitude of expression,

> "He looks
> Quite through the deeds of men;"

and with somewhat of a similar aptness of remark, it may be said of Mr Patterson, he looks quite through the composition of an artistic work, and to a nicety can tell how far it agrees or disagrees with the philosophic canons of true art. More than this, he possesses a singular and pleasing facility in dressing his views so as to present them to the mind's eye with vividness and grace. . . . The volume will form a valuable acquisition to any library.

Church and State Review.

Mr Patterson has long been well known in the world of journalism as an accomplished and elegant writer. The present collection of Essays testifies to the justice of such a representation, and moreover displays the wide range of his knowledge and the superiority of his judgment. His previous work upon the Napoleonic Policy in Europe—though a masterpiece of acute reasoning, and a model for the writing of a political tractate—gave his readers no reason to expect the knowledge possessed by the author in Æsthetics, as well as in the less known

fields of History. Mr Patterson may serve as an illustration of a theory which we are inclined to maintain—namely, that the soundest political knowledge is most likely to exist in conjunction with a refined taste and a broad general culture.

Edinburgh Courant.

Mr Patterson's Essays are the results of thought and study; and his volume is well worth the perusal of reading men. His best quality is a comprehensiveness—a power of grasping a subject as a whole—which proves him to have not only a sound but a wide intellect. The papers bring together within a brief compass a very remarkable amount of knowledge and speculation; and the accumulated store is lighted up by an active and lively fancy—so that, in fact, there is nothing heavy in the book, even when the subject is of the heaviest.

Scotsman.

In his generalisations of history, Mr Patterson displays extensive knowledge and much grasp of thought. . . . His forte is pretty hard thought and historical generalisation.

The Scottish Press.

Mr Patterson is a writer of unusual depth and brilliancy; and he possesses the power of reproducing his thoughts in new forms, and in clear and eloquent language. His penetration and vast range of information, his fine appreciation, his enlarged and genial sympathies, and above all—at least as regards effect—his rich, rolling, and often grandly picturesque style, render him a writer of rare attractions, and, in his own domain, give him a place second to none of our popular authors. . . . One point has especially impressed us—*the extent and definiteness of the author's information.* This is seen on every page: in almost every sentence there comes in some fact or incident or allusion which illustrates the page, and perhaps throws a flood of light on some important question or previously beclouded circumstance. . . . Mr Patterson has invested History with a living interest, and Art with a living beauty. . . . In the Essay on "Real and Ideal Beauty," Mr Patterson combats the Association theory in Art with a power and an eloquence which all will acknowledge. The Essay reads like a poem,—with this addition, that it is full of facts, and bears the stamp of a philosophical and logical mind. We have met with no recent critic who can represent Art in such tangible and attractive forms, and who in its discussion evinces such rational and enlightened appreciation.

Ayrshire Express.

A thoughtful, edifying, and ennobling volume. Mr Patterson is none of those perfunctory litterateurs-of-all-work, useful enough in their way, but with no pretensions to culture or scientific exactitude, who so industriously and ingeniously get up what is known as the "padding" of the magazines. A man of fine natural powers, developed by practice and disciplined by hard study, he treats every subject he undertakes with a consciousness of strength refreshingly free from presumption and dogmatism. Before you have been long in his company, you are

constrained to feel that you are holding communion with a mind equal to everything with which it attempts to grapple. The versatility that originally repelled you soon asserts an overmastering influence, which first interests and then charms. Turning from the subtleties of Art-criticism, out of mere curiosity, you wander into the regions of Historical disquisition to find that there your Mentor is himself, and has the faculty of making you, quite as much at home. . . . So much for the speculative department of the volume. The practical has even stronger claims on our attention and approval. Our author has the rare faculty of applying his extensive reading to great purpose, and of conducting an historical narrative in such a way that the reflections interspersed do not mar its continuity or detract from the general effect. His papers on India and China are masterly in the extreme, affording a fine and informing glimpse of the peculiarities of these two colossal empires. Indeed we do not know where so much valuable matter relating to the customs and recent changes in both can be found compressed within the same limits.

Dundee Advertiser.

A valuable book. Mr Patterson is one of a class of writers which is not increasing. He brings to his work an amount of careful study seldom found in these times. His Essays are not dashed off, like the productions of the scene-painter, to charm for an idle hour; but are like the works of those old builders who never forgot that they were building for all time. He is a workman of the highest class. Like the granite workers of Aberdeen, he may not get on so fast as his brethren in the stucco department; but then his material carries an exquisite polish, and lasts for ever. Sober thought and accurate information, expressed with a quiet, chaste elegance, are the great attractions of these Essays. The reader feels that the essayist is a scholar, a thinker, a man of fine intellect, of amazing information, of indefatigable industry, and of the most cultivated tastes. It is rare that a writer so learned exhibits his learning with so much grace of manner,—or that one so thoughtful clothes his thoughts with so much elegance of expression,—or that one labouring amid such an embarrassing wealth of facts as he evidently has at command can with such a poetic play or fancy adorn his work. There is a fervid, gushing eloquence in all the papers where the nature of the subject admits of the author giving the reins to his imagination. His Essays have all the attractions of those Greek temples, with whose harmonious proportions, vast strength, enduring substantiality, and elegant decorations he is in love.

THE ECONOMY OF CAPITAL.

(1864.)

CONTENTS.

I. Thoughts on Gold.—II. What is Money?—III. The Golden Age. Effects of the Gold-Discoveries.—IV. The Economy of Capital. Banking. Monetary Crises.—V. The City of Gold.—VI. The Bank of England. Our Monetary System. Defects and Remedies.—VII. Our Trade. What is Over-Trading?—Appendix. Position of the London Joint-Stock Banks. Comparison of English and Scotch Banking. What is a Pound? &c.

Morning Post.

A volume which will be hailed with pleasure by the entire commercial community. It displays throughout a thorough acquaintance with our Monetary System, and is written in the lucid and graceful style which distinguishes Mr Patterson's works. . . A work replete with interest and information,—and which, apart from this consideration, would repay perusal on the ground of its literary merits, and the graphic pen-pictures with which the author has illustrated his subject. . . . The reforms requisite to bring our Monetary System into harmony with the spirit of the age and the requirements of the community, are ably pointed out.

Morning Advertiser.

In the foremost rank of Metropolitan literary workers the author of the present volume has a place. He has gained this honourable position, and sustained it well, by his nervous and lucid style of writing, and by his extensive knowledge bearing on the great practical questions of the time. . . The chapter on the Bank of England contains a full exposition of our Monetary System, and of the reforms that are considered requisite. The chapter is masterly; it is a complete history of itself, and well deserves the study of every one engaged in mercantile affairs. . . A very interesting Appendix concludes a volume of rare merit.

Westminster Review.

In all that really has reference to the Economy of Capital, Mr Patterson's book is most excellent. His information is complete; his style is clear, forcible, and even picturesque; and his account of the modes by which capital is economised in the banking system, is the very best extant; but his theory of what that system should be is open to the gravest objections. . . His account of the effects of the gold-discoveries of California and Australia, of the Economy of Capital, and of the money-market—or, as he calls it, "the city of gold"—is most masterly and judicious. These chapters are singularly accurate, clear, and succinct. . . On banking proper, he is an excellent guide and authority. . . The utopia of money without means must be attractive indeed to delude so clever and accomplished a writer as Mr Patterson; but utopian or not, there are few books on the subject better worth reading than his.

Bell's Weekly Messenger.

This is not only a well-timed book, but it is one which completely exhausts the long-debated subject of currency. It seems scarcely possible that any one following Mr Patterson through all his arguments, deductions, and explanations, can any longer hold to the opinion, that the system at present in force can be advantageous to the country. . . . We never saw the full force of the anomaly of the present system so clearly until we followed Mr Patterson chapter by chapter, and page by page, through his highly instructive and most important book. . . . No writer has grappled with the whole subject with a more firm and resolute determination.

The Index.

This is one of those books which defy the art of the reviewer. Facts will not bear squeezing, and facts constitute the true value of this work. The best advice that can be offered is that the book itself should be read: and this advice can be justified without difficulty. For here we have a combination of an essay, or series of essays, on the theory of Capital, on trade in Money, and on Banking, together with an admirable polemic directed against the Bank Act of 1844, and also with a Monetary and Commercial Dictionary. Again, we have a book which will go far to popularise the above-named sciences,—to unfold what every man at a distance of half a mile from the Royal Exchange regards as an inexplicable mystery; while at the same time we have an attack on the system of Sir Robert Peel, and indeed on the system of English banking, which would task the efforts of the occupants of the bank-parlour to defeat.

Morning Herald and Standard.

Mr Patterson has a happy faculty of writing not only strikingly but suggestively. His mind has breadth as well as force. His views are always large; and his style is singularly free from obscurity and dryness. We are mistaken if the volume does not excite the attention of merchants generally to the questions it discusses, and gain for its author a high position among the most successful expounders of the difficult and abstruse problems of Monetary Science.

British Quarterly Review.

A very brilliant chapter of Mr Patterson's volume is devoted to the City, and to the business carried on therein. . . It is like the effect of the pictures of London recently painted by the lamented David Roberts. We feel almost as if we heard the roar of the ceaseless traffic, and joined in the restless activity, as we read Mr Patterson's descriptions.

Money-Market Review.

A work which constitutes a full and complete exposition of our whole monetary system. But it is more than that ; for, although it contains very lucid and very able and philosophical expositions of trade and commerce, of banks and banking, and of money and capital, the book is really a very readable and most interesting book. It is just such a work as all men engaged in trade, or interested in commerce or banking, ought to read ; and it is a work containing just such matter, communicated in such a light and lucid style as is most likely to tempt and best calculated to repay its perusal.

St James's Chronicle.

The present state of financial affairs is calling attention to Mr Patterson's remarkable work on 'The Economy of Capital.' Both in finance and politics Mr Patterson has a semi-prophetic faculty. He has predicted both the career of Napoleon and the crises of the money-market. The volume to which we refer, published in 1864, reads like a commentary on the Panic of 1866. Curiously enough, he has succeeded in making the subject interesting by the fascination of his style : a Bank Manager described the effect of the book upon him as "studying finance to the sound of music."

The Cosmopolitan.

Mr Patterson's book was published long before the financial panic of 1866, yet it reads like a commentary on that memorable and disastrous event. . . We earnestly commend this exhaustive work to the careful consideration and study of those who are interested in the growth and development of the commerce of England. Mr Patterson knows more fully what he writes upon than nine-tenths of the bankers, discounters, and monied men of London. We deem it desirable that the works of so able a writer should be known to the financial world.

Liverpool Albion.

A work whose arguments cannot fail to arrest, as its facts cannot fail to instruct. . . Mr Patterson has evidently an inheritance of the 'faculty of money' and the logical acumen which were combined and exemplified in such a remarkable degree in Adam Smith. . . His statements and deductions are based on observations made for the last fifteen years, and are entitled to the fullest consideration. . . There is poetry in the author's portrayal of the good and the glory of Commerce,—and of the toil in the lands of the sun and snow, of Australia and Siberia, for gold, the magician of trade. But the book has an

entirely practical bearing; and in the 'Golden Age' is delineated the flow of emigration—the financial relieving of Europe—and the extension of operations produced by the influx of new golden store. . . The research into the cause and cure of various panics must be read to be appreciated; and it would be well if banks and the public would consider the suggestions made for their mitigation or avoidance.

The Citizen.

Mr Patterson's great work.

The Press.

Mr Patterson does not hesitate to assert that the principles of monetary science, as generally received at present, are radically wrong,—that they are founded on a total misconception of the nature of that science,—and that posterity will assuredly pity our folly and barbarism in having been so long misled, and thereby incurring such widespread suffering and even national disaster. We believe it impossible for any impartial advocate of the present system to study with attention Mr Patterson's arguments and not confess that he is right. In doing so he will be greatly assisted by the eminently lucid and concise manner in which the author has stated his case. His style is everywhere neat and condensed, perspicuous and graceful, and not a doubtful or obscure passage is to be met with throughout the volume. These are the signs of a clear and deep thinker, who sees through and through his subject, and is accustomed to contemplate it from every possible point of view. . . A most difficult subject has been treated by Mr Patterson in a manner which, we feel sure, will be not only intelligible but agreeable even to the general reader. He displays his great powers as a vivid and picturesque writer in close and interesting contrast with the highest powers of a profound and concentrated thinker.

Leeds Intelligencer.

A wonderful work. A book that will in a few years be not only in every English library, but will have a world-wide reputation. It is no dry synopsis of the state of Money and Trade, but rather an historical novel on a subject which engrosses the attention of almost every person alive. Step by step Mr Patterson proceeds—each successive chapter further developing the subject, vying with one another in interest, and impressing upon the mind that, vast and comprehensive as is the subject, the intellect, penetration, and accurate information of the author are fully equal to the task of engrossing the reader, and enabling him thoroughly to grasp the subject. The chapter on the 'City of Gold' is a series of the most exquisitely drawn pictures in the heart of the metropolis, in the painting of which the hand of genius is plainly visible. Not only are we dazzled by the brilliant colouring and life-like reality of each particular picture, but we are especially struck by the depth of thought, and the extent and definiteness of the author's information. . . Acute reasoning, and a wonderfully rich and graphic style, combined with the fact that the author brings before us nothing but simple truths, stamp Mr Patterson as a man of sound judgment, unequalled in speculative philosophy, thoroughly practical, and indefatigably industrious.

Glasgow Herald.

A very readable book, peculiarly well timed. . . The subject is very ably handled by one who has evidently given it careful study, and bestowed upon it a considerable amount of labour in the collection of facts, by which he clenches his arguments in support of free trade in banking and currency. . . The chapters on the 'Bank of England' and the 'Economy of Capital' are decidedly the best. The criticism on the Bank Acts is searching, thorough, and complete.

Edinburgh Courant.

Mr Patterson has done some remarkable literary feats in his time, but scarcely any so remarkable as the composition of this volume,—in which the Currency question is handled not only with originality and vivacity, but absolutely with attractive picturesqueness. In proof of its originality, we may point to the passage in which one value of the Gold-discoveries is shown to be, that they permitted the vast extension of our imports from the East,—imports which had to be paid for in silver, and which could be so paid for only because gold flowed in from California and Australia to replace the silver flowing out.

Dundee Advertiser.

Works on Political Economy are so uniformly dull that it is really quite a relief to come across a book like this, which carries you along almost in spite of yourself. The 'Economy of Capital' is a book which is sure to attract attention ; and from the exhaustive manner in which the subject is treated, it cannot fail to have weight and importance. The commercial man will find it replete with useful hints—the political economist will discover many golden maxims,—while the general reader will find a mass of information conveyed in a style both terse and attractive.

North British Daily Mail.

A good book on the joint subject of our Monetary and Trade systems. . . An excellent work, full of clear and admirable maximic sentences, weighted with meaning, and which cleave to the marrow of a difficult question. . . We commend Mr Patterson's book to the English and Scottish Chambers of Commerce, to our Parliamentarians of both Houses, and to the commercial world.

The Irish Times.

Mr Patterson is not a writer from any mere speculative whim. He has taken up, and brought his extensive journalistic experience to bear upon, a subject affecting largely the social progress of the age, and having its basis in the soundest principles of political economy. If he is at any time speculative, he is also suggestive, and he invariably follows up the propounding of a theory with pointing out a practical deduction. To deal efficiently with a subject requiring so large an accumulation of facts implies on the part of the author superior judgment, acute reasoning power, and great subtlety in analysis. These qualities are pre-eminently remarkable through Mr Patterson's work. And perhaps, after the judicious arrangement of the materials at his dis-

posal, there is nothing stands so prominently forward as its wonderful *concentration*. Considering that the subject is one in relation to which such extensive research is required, of which so clear and thorough an elucidation is necessary, and which, in consequence, demands the most comprehensive and elaborate treatment, every statement and argument of the writer seems to be confined to the smallest possible limits. But this is a concentration without the semblance of confusion, and utterly free from any crowding or ambiguity. How so densely-packed information may be communicated with such pleasing results, and with a power so sustained and clearly defined, may seem a matter of wonder; but the author of the 'Economy of Capital' is a clear and deep thinker, and always thinks and writes in order. He is terse and uniform in his statements, graphic and forcible in expounding his views; and whether exposing a fallacy or urging an argument, he never violates any logical canon. Mr Patterson commences his book with a chapter containing 'Thoughts on Gold,' in which his observations are so strikingly original, yet so *apropos*, that the reader begins to wonder why the matter has not previously engaged his attention. His sympathies are thus gradually enlisted, and he eagerly peruses the work through its different stages of development. To give anything like an adequate idea of a work so comprehensive within the limits of a review were more than a herculean task. The book, to be appreciated, must be read, and followed from stage to stage of its logical and argumentative development. Books on similar subjects are frequently too heavy to suit the majority of readers, but what is often a true result is not always a necessary consequence, and Mr Patterson's volume is a very decided exception. Grace, elegance, and vigour are its principal characteristics, and interspersed through the work are descriptive passages worthy of the best literature of the day. Versatile without flippancy, he is learned without being pedantic, and argumentative without an approach to dogmatism. The Laureate, in one of his noblest poems, lauds the progress of the nineteenth century, and tells us that we are only 'in the morning of the times.' If it be so, and if other intellects in the land are so usefully employed in developing our progressive tendencies as is Mr Patterson in the excellent work we have been reviewing, we may reasonably anticipate a glorious noon-day.

William Blackwood & Sons, Edinburgh and London.